The Incorporated Accountants' Journal

The Official Organ of
The Society of Incorporated Accountants and Auditors

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Professional Notes.

THE outstanding events of the past month have been, first, the announcement of the success of the War Loan Conversion scheme, which has resulted in £1,850,000,000 out of a total of £2,087,000,000 being converted up to the present time, and, in the second place, the success of the Ottawa Conference after a month of strenuous negotiations. The full particulars of the agreements arrived at are not yet available, but so far as they have been disclosed they appear to have given general satisfaction, and the delegates themselves state that what has been accomplished marks a degree of success far beyond anything that was expected before they left England. On the arrival of the British delegates at Southampton they were welcomed on behalf of the Corporation by the Mayor, Councillor F. Woolley, Incorporated Accountant. A short account of the proceedings on the occasion will be found in another column.

We publish this month extracts from the Report of the Committee of Enquiry into the affairs of the Post Office. The report is a long one, and we have accordingly selected the portions relating mainly to accounts and finance, together with the general conclusions arrived at by the Committee. One of the recommendations of the Committee is that the accounts of the Post Office should be put on a revenue as distinct from a cash basis, and that it should pay for services performed for it by other departments, and receive compensation for services rendered to other departments. The opinion is also expressed that the separation of the Accountant-General's department—with the general efficiency of which the Committee is very much impressed—has resulted in financial control being to a large extent confined to the exercise of *ex-post facto* criticism instead of manifesting itself by active participation in the administration.

The proceedings of the Incorporated Accountants' London and District Society will open on Wednesday, October 12th, with a luncheon at Incorporated Accountants' Hall, on which occasion the President of the Parent Society, Mr. E. Cassleton Elliott, will be the principal guest. Other items in the syllabus, which we publish this month, are a lecture by Professor Gregory, D.Sc., on a subject to be announced later, a lecture by Lord Melchett on "Accountancy Methods as a Factor in the Economic System," and at a later date another luncheon, at which the principal guest will be Dr. Cyril Norwood, Head Master of Harrow School.

The Chamber of Commerce of the State of New York has been discussing the practice which prevails to some extent in America of company auditors being elected by the board of directors or the management in place of their being appointed by the company in general meeting, and the Chamber has passed the follow ing resolutions:—

That the Chamber of Commerce of the State of New York urges upon the directors

of all corporations whose accounting methods are not under federal or state supervision, but whose securities are dealt in publicly, to amend their by-laws to require that independent certified public accountants shall be selected by the shareholders; that the reports of such accountants shall be rendered in full to each and every director and be made available for inspection by the shareholders; and that the text of the accountants' certificate be spread on the minutes of the company and printed in the annual report; and

That the chamber recommends that all close corporations and firms, as well as counties, cities and other political sub-divisions which require substantial loans from financial institutions or others, inaugurate the practice of periodical audits by independent certified public accountants.

Our readers are probably aware that in America the term "corporation" mentioned in the resolutions is used as applicable to trading companies as well as to other corporate bodies.

The case of *Koch* v. *Dick*, heard in the King's Bench Division last month, shows the danger of making any alteration in a Bill of Exchange, after acceptance, without the consent of the acceptor and any other interested party. The bills in question in this action purported to be drawn in London and were accepted and returned to the drawers in that form. They were subsequently endorsed by the drawers and passed over to Mr. Koch for value. In order to get the bills discounted by a German Bank, the word "London" was altered to "Deisslingen," thus changing the bills from inland bills to foreign bills, without any communication being sent to the acceptor. On presentation for payment the bills were dishonoured, and the Court held that, as the alteration was material, the bills were consequently avoided under sect. 64 of the Bills of Exchange Act, 1882, which provides that where a bill is materially altered without the consent of all parties liable, the bill is avoided except as against a party who has assented to the alteration. Judgment was accordingly given for the defendant, and Mr. Koch was unable to recover.

An interesting point in relation to share transfers came before Lord Moncrieff in the Court of Session at Edinburgh, in the case of *National Bank of Scotland* v. *Askit Limited*. A transfer of certain shares in the company was passed without a formal meeting of the directors, but with the verbal assent of three out of the four members of the board. The transfer was registered in the company's books, and the secretary issued an intimation to that effect. It was claimed by the company that the passing of a transfer other than at a meeting of the board properly convened could not have legal effect, and that the right of the plaintiffs as transferees of the shares was accordingly incomplete. His Lordship refused to accept this view, and found that the right to the shares vested in the bank's nominees.

The case of *Thomas Merthyr Colliery Company* v. *Davis* (*Inspector of Taxes*), referred to in our Professional Notes of July last, has now come before the Court of Appeal, and the judgment of Mr. Justice Finlay has been affirmed. The point at issue related to the right of the company to charge, for Income Tax purposes, subscriptions paid to a Coal Owners' Association by way of calls upon members in relation to stoppage of output caused by strikes. The Master of the Rolls, in delivering judgment, said there were many classes of expenditure which a prudent director might incur which were not admissible deductions. The dictates of prudence were not the true test. The question for decision was whether there had been any alteration in the decisions of the Courts since the case of the *Rhymney Iron Company, Limited*, v. *Fowler* in 1896, such as to make that case no longer binding. He could find no such decisions and accordingly held that the subscriptions in question were not admissible charges.

A curious case came before the Liverpool Bankruptcy Court the other day. A receiving order had been made against an elderly woman, because she had refused to pay her Income Tax and Sur Tax, although she proved to be possessed of about £80,000, which stood to her credit in various banks in Liverpool, in addition to some investments. The Inland Revenue Department was the only creditor, and the Official Receiver stated that he proposed to pay the amount due as quickly as possible, and then apply for annulment of the bankruptcy. A similar experience occurred with the same person in the year 1927, when a receiving order was made against her in the High Court in London. The Official Receiver stated that the debtor would not see him or his solicitors, and ignored all proceedings and all orders of the Court. She was obsessed with the idea that she was a very poor woman and lived on 30s. a week.

The position of a landlord in regard to obtaining possession of rooms which a statutory tenant has *bona fide* sub-let at a rent which includes payment in respect of "board, attendance or use of furniture" has now been settled by the decision

of the House of Lords in the case of *Barrell (Pauper)* v. *Fordree*. The tenant had sub-let to one person three rooms partly furnished and to another two rooms fully furnished, retaining two rooms for his own occupation. Having received notice to quit, he became a statutory tenant, and the effect of their Lordships' judgment is that the house was divided into three separate dwelling-houses and that two of them, being sub-let furnished, were excluded from the operation of the Rent Restriction Acts and the landlord could therefore recover possession of them under his common law right. The statutory tenant was held to be entitled to retain the rooms which he actually occupied, the rent being apportioned between those rooms and the rooms which he had sub-let.

Representatives of building societies had a meeting in London recently for the purpose of considering the question of reducing the rates of interest on moneys advanced on mortgage. There was a full discussion on the subject, but no decision as to any change was arrived at. This has caused a little surprise, because some of the northern and midland societies have indicated their intention of lowering the rates of interest charged to borrowers, although the rates now in force in these societies are already lower than those in the Metropolitan district. It was explained by Sir Harold Bell after the meeting that there were special problems affecting different societies which had to be investigated before full agreement could be arrived at, because conditions in the south of England were entirely different from those in the north, and it is understood that a further meeting will be held shortly. The question of reducing the rate of interest payable to investors was also discussed in relation to its bearing upon rates of interest to be charged to borrowers, and it transpired that there was considerable difference of opinion upon the point.

The official general summary of the operations of building societies in England, Wales and Scotland for the year 1931 will not be published until later in the year, but certain statistics compiled from advance information supplied by the Chief Registrar of Friendly Societies to the National Association of Building Societies shows that the total liability to depositors and creditors has increased by about £6,400,000 as compared with the year 1930, and that the liability to shareholders has gone up by £39,000,000. While the number of societies has somewhat decreased the number of accounts under all heads has substantially increased. The total receipts, which amounted to £169,000,000, are about £1,000,000 down, but the advances on mortgage have gone up by £1,500,000.

Two directors of a financial corporation were fined £50 each and costs by the Lord Mayor of London recently for having contravened sect. 354 of the Companies Act, 1929, by issuing a form of application for shares unaccompanied by a prospectus. There was no allegation of fraud, but it transpired in the course of the hearing that the company for which the parties were acting was to receive a remuneration of 25 per cent. on the value of the shares sold. His Lordship said that, as Parliament had fixed the maximum penalty at £500, he must treat the offence as a serious matter, and he ventured to think that if any recipient of the circular had been told that out of every £100 worth of shares he purchased £25 was to go into the pockets of the people asking him to buy, he would not have given it a moment's consideration.

It is announced that in the first five days 746,257 of the new series of Savings Certificates were sold. This is a remarkable achievement, having regard to the appeal in connection with the War Loan Conversion and in the absence of any advertising by the National Savings Committee. The issue price of the certificates is 16s. and the value will increase to 23s. after eleven years. The increase per certificate at the end of each year will be 8d., except in the first two years, when it will be 4d. per annum only, and in the last year, when it will be 1s.

In answer to a question in the House of Commons, Mr. Baldwin stated that holders of stock of the 3½ per cent. War Loan would be chargeable to Income Tax for 1933-34 on the amount of their dividends for that year and not by reference to the dividends for 1932-33 on their corresponding holdings of 5 per cent. War Loan. Mr. Baldwin said he was glad to have the opportunity to make the matter clear, as there seemed to be some doubt upon the point.

The Government has just announced its intention to repay the outstanding portion of the 4½ per cent. War Loan of 1925-45 and the 4½ per cent. Treasury Bonds, 1933-34. The amount of the former is nearly £13,000,000, and the latter £140,000,000. How the necessary provision is to be made is not indicated, but it is anticipated that another refunding operation will be announced about the month of October. Meantime the restriction on new capital issues is to be modified to some extent. The Chancellor of the Exchequer has stated that he would be glad if

not more than the following operations were undertaken until October 1st, when the question of terminating the restriction will be considered :

(*a*) An exchange of one class of security for another without change of ownership.

(*b*) An issue of a new security to replace the final redemption of another which had, prior to July 1st last, been fixed for a date earlier than December 1st next.

The proviso is added that these operations shall concern only British (including Empire) sterling issues domiciled in London and shall not involve underwriting nor the provision of new cash.

In relation to the present trade depression in America, the *Journal of Accountancy*, New York, under the heading "We might rejoice in tribulation," makes the following comment :—"Someone said the other day that the Americans are bearing their burdens stoically. There is no general unrest. There are practically no strikes—as indeed there could hardly be when there is no work. There is no breathing out threatenings and slaughter against the Government. We simply endure and hope for fair weather. But there is another way which might be better yet, and it seems that the British in this are showing us how to fare. It has been the admiration of the whole world that in spite of its terrible burden Britain seems to be getting her head above the waves, and this is attributed by many careful thinkers to the fervour of the people. They seem, most of them, to be imbued with a real desire to pay and be done with it. They are going down into the depths of their pocket books and paying taxes far greater than we have ever paid in this country, and they are doing it with what seems like eagerness in that same spirit of getting done with it. If Americans would adopt the same patriotic sentiment and each one of them do everything possible to make and maintain a balance in finance it would help us enormously out of the storm."

According to the figures of the American Federation of Labour, which are based on Government information, the total number of unemployed in America at the present time is estimated at more than 11,623,000, in addition to which there are approximately 760,000 in temporary employment on farms who will be unemployed again at the end of the summer. The President of the Federation estimates that if unemployment continues to increase at the present rate there will be well over 13,000,000 out of work by January, 1933, and that at the present time there is only 30 hours work a week for each if all who want work are employed.

BENEFIT OF EXECUTION IN BANKRUPTCY.

THE Bankruptcy Act, 1914, sect. 40, provides that where a creditor has issued execution against the goods or lands of a debtor, or has attached any debt due to him, he shall not be entitled to retain the benefit of the execution or attachment against the trustee in bankruptcy of the debtor, unless he has completed the execution or attachment before the date of the receiving order, and before notice of the presentation of any bankruptcy petition by or against the debtor, or of the commission of any available act of bankruptcy by the debtor.

If a receiving order is made against a judgment debtor, and the writ of execution has not been carried out to completion at the date of the order, the property taken under the execution and the fruits thereof pass to the trustee in bankruptcy of the judgment debtor for the benefit of the general body of creditors. Where the execution creditor has received any money or benefit under the incomplete execution, he cannot retain, as against the trustee in bankruptcy, the benefit so received. In *Re Ford* (1900), execution having been issued upon a judgment for £80 and costs, the Sheriff, on December 31st, 1898, levied under a writ. On January 5th, 1889, the debtor, under an arrangement with the solicitors of the execution creditors, paid the solicitors a sum of £40 on account, and gave to the Sheriff authority to re-enter under the writ upon default in payment of any of the instalments of the balance at the agreed dates for payment. The Sheriff thereupon withdrew. On January 14th a receiving order was made against the debtor on his own petition. At that date the Sheriff had not re-entered under the writ. It was held that the execution had not been completed as to the £40 at the date of the receiving order; that the execution creditors were therefore not entitled to retain the benefit of the execution; and that the trustee in bankruptcy was entitled to the £40 as part of the debtor's estate.

If there has been only a partial execution, a levy and no subsequent completion, the intention of the Act of 1914 apparently is that the other creditors may step in and insist on having the whole of the debtor's estate rateably divided. The test seems to be whether or not the execution has been partial only—that is, whether or not a partial benefit has been obtained from it. It seems that if the execution creditor gets a partial benefit, but retains anything in the nature of an incomplete execution, then he cannot retain the

partial benefit which he has already received. If the respondents in the above case had accepted the £40 in full satisfaction of the debt, and had not claimed a right to re-enter at some subsequent time and go on with the execution, then they might have retained the £40. It would have been the same as though instead of £40 they had received the whole £80 through the Sheriff, which they clearly might have kept. But they claimed to have the benefit of an execution which was kept standing over, and which was incomplete, and sect. 40 means that where the execution creditor is taking such a benefit the general creditors may come in if they can avail themselves of any act of bankruptcy, and may have the property distributed rateably, and prevent the execution creditor from getting any benefit from an execution which is only partial and incomplete.

In *re Brelsford* (1931), judgment for £215 was recovered by the M. Co. on September 17th, 1928, against the debtor, who afterwards became bankrupt. On the following day the Sheriff levied execution on the goods of the debtor under a writ issued by the company for their judgment. On September 24th, 1928, it was agreed in writing between the company and the debtor that in consideration of the company withdrawing execution, the debtor should pay to the company £15 on account of the debt and the balance thereof by monthly instalments of £10 each, the debtor undertaking, in case of default in payment of any of the agreed instalments, to authorise the Sheriff to retake possession. In pursuance of the agreement, the £15 and the costs of the execution were paid, whereupon the Sheriff withdrew. Up to October 22nd, 1929, the amount paid in respect of the instalments was £63, and on January 10th, 1930, the Sheriff entered a second time into possession to levy execution for the balance of the debt remaining unpaid. On January 13th, 1930, while the Sheriff was in possession, a receiving order was made against the debtor on his own petition, and he was adjudicated bankrupt. The following day the company received notice of the receiving order, and two days later the trustee in bankruptcy claimed payment of the two sums so received by the company, amounting to £78, as forming part of the bankrupt's estate available for the general body of his creditors. It was held that if the company retained the £15, they would be retaining some part at least of "the benefit of the execution" within the meaning of sect. 40, because they had obtained payment of that sum only as the price of their allowing the Sheriff to withdraw. As to the £63, that sum which was obtained as the price of not allowing the Sheriff to re-seize the goods, was also a sum which, if retained by the company, would be part of the benefit of the execution. The company therefore were bound to account to the trustee in bankruptcy for both sums in dispute.

EXECUTOR'S RETAINER AND CROWN'S PREFERENCE.

THE name of Cockell is likely to be known by a generation of accountants in practice, and to more than one generation of students, as the decisions which have been given as a result of the state of that gentleman's affairs are of extreme importance. The latest development arose in the case of *In re Cockell; Jackson* v. *Attorney-General*, which was referred to briefly in our Professional Notes last month.

Cockell died insolvent owing eight years arrears of Income Tax and two years' arrears of Super Tax, in addition to other liabilities. He was even indebted to his sole executrix, and it was this debt which gave rise to the litigation that commenced shortly after his death. In the first place, the executrix contended that she was entitled to retain what assets there were, and to apply them to the discharge of what was owed to her by the estate. The argument whereby she supported this contention was ingenious. Sect. 34 (1) of the Administration of Estates Act, 1925, provides that, where the estate of a deceased person is insolvent, the assets are to be applied in discharging the debts in the order prescribed by Part I of the First Schedule to the Act. This Schedule provides that, where the estate is insolvent, the assets are to be applied, first, in paying the funeral, testamentary, and administration expenses, and then in paying the debts which would be entitled to preferential treatment in a bankruptcy.

To a certain extent a claim in respect of arrears of Income Tax is entitled to preferential treatment in a bankruptcy, and it appeared, therefore, that some of the arrears of tax should be paid before the debt due to Cockell's executrix, since that debt was not entitled to preference. But the executrix contended that, in spite of sect. 34 (1) and the First Schedule, she was entitled to exercise her power of retainer. The Crown objected on the ground that, though an executrix has a power of retainer, she is entitled to retain only as against other debts *of the same degree*, and that, as some Income Tax was preferential, their claim was a debt of a superior degree to that of the executrix in question. This objection was countered by an ingenious argument, which need not now be examined in detail,

but it was so ingenious that the Judge in the Court below found in favour of the executrix, and ruled that she was entitled to exercise her power of retainer. This ruling was subsequently over-ruled by the Court of Appeal and the House of Lords, the ultimate result of the dispute being that, in so far as the Crown would be entitled to preferential treatment in a bankruptcy, the Income Tax owed by the estate was a debt against which the executrix was not entitled to exercise her power of retainer.

But this was not the end of the dispute, for the Crown claimed that they were entitled to claim preferential treatment in respect of the best year's tax, and were not obliged to take payment in respect of the most recent year's tax. This point had not previously been argued definitely, though in earlier cases there were dicta in favour of the Crown's contention.

Perhaps the most important of these earlier cases was *Gowers* v. *Walker* (1930), in which the Crown's right of preference upon the appointment of a receiver was considered. In this case an assessment was made on the company after the receiver's appointment in respect of the financial year ended April 5th preceding the receiver's appointment, and it was held that the tax due in respect of that year was a preferential debt. This decision seems only remotely connected with the point in *Cockell's* case, but the Judge decided that it obliged him to give a ruling in favour of the Crown, and an order was accordingly drawn up in the following form :—

" This Court doth declare that the preferential claim of His Majesty for property or Income Tax can be made for property or Income Tax assessed for any one year ending on any 5th of April before the testator's death."

The importance of this order to executors, receivers, trustees in bankruptcy, and liquidators needs no emphasis.

THE INDEPENDENCE OF AUDITORS.

The following article appeared in *The Statist* of August 8th, and is reproduced by permisson :—

There has been considerable discussion recently in accountancy circles on the question of amendment of company law with a view to defining and clarifying the duties of auditors, particularly in connection with the accounts of large companies. Professional opinion seems to be divided as to the necessity for such amendment, one school of thought inclining to the view that auditing practice should be standardised as much as possible, that auditors' duties should be reduced almost to an exact science so far as legislation can do so, and that as little as possible should be left to individual discretion. The other apparently believes that the lesson of the *Kylsant* case will not be lost either upon individual auditors or upon the trend of thought of the profession as a whole, and that it can safely be left to the profession itself in practice to bring about the desired reforms. If the aims of the first school were to be achieved, presumably a further Parliamentary Committee would have to examine the whole question most carefully, and if the fate of the recommendations of the previous committee is any criterion it is very doubtful whether the result would be satisfactory to anybody. In fairness to that Committee it must be said that the bulk of the criticisms which led to modification of their most important recommendations came from those quarters which are now clamouring for further amendment and railing at the futile results of the final form in which the Committee's recommendations were enacted. There is no reason to think tnat the recommendations of another committee, by the time they have run the gauntlet of a mass of ill-informed or prejudiced criticism, both in and out of Parliament, would have any happier result.

It would seem, therefore, that the greater hope must lie in the direction of progressive action in the profession itself, and a more sympathetic outlook on the part of company directors. The need for greater enlightenment of shareholders was emphasised by the Judge in the *Kylsant* case, and his warning, as well as the moral of the case generally, should form a very useful argument in support of auditors with which to impress directors of companies who attempt to arrogate to themselves any functions properly belonging to the auditors. No doubt in the past auditors have been reluctant to maintain their own views against the wishes and opinions of directors where those views derived no legal support from the Companies Act, but it may be argued from the *Kylsant* case that a too blind reliance on the letter of the law in such matters, particularly if persisted in over a long period, may eventually put both auditors and directors beyond the protection of the law, or at any rate in the invidious position of having to seek it. It may be expected, therefore, that directors will in future be more disposed to have due regard for the reasonable requirements of shareholders in framing their accounts, and auditors' views thereon. Whether those views should be standardised and enforced by concerted action on the part of the profession as a whole, or left to the individual discretion of auditors, must be a matter for decision by the various professional bodies, but here again there appear to be divided counsels. In any event it is to be hoped that, failing general agreement as to the best tactics, the more important firms will give a lead in this cause.

That this hope is not a vain one seems to be borne out by the more positive attitude taken up by auditors as evidenced by the altered tone of auditors' reports in several recent cases which have come to our notice. Instead of the stereotyped certificate which had come to be almost meaningless it is now by no means unusual to see a number of qualifications, and

in one notable case amongst those referred to the qualification was such as to invite an expression of opposite opinion in the directors' report. This is a welcome indication of a more conscientious attitude on the part of auditors with regard to their duties towards shareholders, and of greater independence in their relations with directors. Whether this new conception of auditors' responsibility is sufficient to solve the thorny problem of the information to be furnished regarding subsidiary companies, including sub-subsidiary companies, is more doubtful, and it should be noted that under the Companies Act auditors have primarily no responsibility in this connection. The present legal requirements on this matter, whatever may have been their intention, have in practice been interpreted in a manner which can only be described as fatuous, but although there appears to be unanimity as to the need for revision of this practice, by legislation or otherwise, there is by no means unanimity as to the form which such revision should take. It is satisfactory to note that the consolidated balance sheet and profit and loss account are being more and more advocated and adopted, but there are no doubt many cases where a consolidated balance sheet may be almost impossible to prepare, and may even be misleading. There seems, however, to be no reason why alternative methods should not be employed, according to the circumstances of each case, for giving shareholders the information they are entitled to. For instance, in some cases it might be more convenient to furnish the separate accounts of subsidiary companies with particulars of the parent company's interest in them. The main concern, however, of the shareholders of such a company is earning capacity, and in most cases they would be satisfied with information as to the total earnings of subsidiary companies, the proportion of those earnings applicable to the parent company's shareholding, and the dividends from subsidiaries included in the parent company's profit and loss account. We ourselves do not see any real necessity for furnishing this information in respect of each subsidiary company any more than if each company were a branch, nor, except for the light which it throws on the liquid capital position, is the aggregation in a consolidated balance sheet of assets and liabilities of a heterogeneous nature and value likely to be of great interest. Nor again is it of material importance to know from which subsidiary companies dividends are drawn by the parent company or the relation between dividend and earnings in any particular case, but the one thing which the shareholder or investor does want to know, as the most important index to the true state of affairs, is the earning capacity of the concern as a whole, since the real value of the assets as a whole depends on their earning capacity. We do not overlook certain practical, though exceptional, difficulties such as the treatment of inter-company transactions or of preference dividends or debenture interest of subsidiary companies payable to outsiders where such dividends or interest have not been earned or paid, or may have been paid out of reserve, but there can be no such difficulties of an insuperable nature. The whole of this information might conveniently form part of the directors' report in substitution for, or in addition to, the meaningless statement which is at present required to be appended to the balance sheet, and it might be amplified in respect of such particulars as reserves, liquid resources, contingent losses, &c., of subsidiaries or of the group as a whole. The very least to which shareholders appear to be entitled is that they should know whether dividends paid or proposed to be paid by the parent company are covered by the combined earnings of the group, but even this minimum safeguard, which was recommended by the previous Committee on Company Law Amendment, did not find its way into the Act. Until some such reform, either of the law or accountancy practice, is brought about, it will not be possible to assume with any confidence that the accounts of large concerns do really show the true state of affairs, and if the accountancy profession can hasten progress along these lines, with or without legal support, it will deserve the gratitude of the whole commercial community.

It is unreasonable, however, for shareholders to expect to be spoon-fed by their auditors, and the notorious apathy of shareholders almost deserves the worst that can befall them. A large proportion of the blame for the disasters that have overtaken many important concerns in recent years must be laid at the door of shareholders who have not troubled to take an intelligent interest in their companies or the management thereof.

WELCOME TO OTTAWA DELEGATION.

A civic welcome was extended to the Ottawa Conference Delegates, upon their arrival at Southampton last week, on board the "Empress of Britain."

The Mayor of Southampton (Councillor F. Woolley, J.P., Incorporated Accountant), speaking on behalf of the deputation, tendered the town's welcome, and said that Southampton had a shipping interest connected with all parts of the British Dominions and he thought he could claim that the townspeople had more than an average degree of interest in the purposes and achievements of the United Kingdom Delegation in collaboration with their colleagues of the Empire. Southampton, he said, shared to the full the admiration and gratitude of the rest of the country for the strenuous efforts that had been made in the interests, not only of consolidation, but of the extension of trade and commerce and that revival for which they were confidently looking. It was significant that the Conference marked a very definite step forward in the development of the relationships between the various parts of the Empire which was bound to make for stability, common understanding and common effort towards securing the interests of all. Continuing, he said : " I do not know what name history will give to the age in which we are living, but I am quite sure of this—that this age will be known as a period in which men of all nations have learned the art of coming together, and that is all to the good

and is bound to make for the best interests of mankind in future generations. If that is true of most of the nations of the world, it is specially true of those nations which form the British Commonwealth of Nations, and we congratulate you and welcome you back to the shores of Old England." Concluding, he said that they would be glad to hear in due course of the work which had been done at Ottawa and to share in the benefits which would accrue.

Mr. Baldwin, in replying on behalf of himself and his colleagues, said: "I would like to assure you of the deep appreciation we have of the honour you have done us in coming—the Mayor, Sheriff and Member of Parliament for this ancient borough—to welcome us on our return to England. We are grateful for all you have said. For ourselves, we have been a very happy and united team. We have not cared who among us made the runs, provided the runs were made. I hope and believe we have done a useful bit of work, and if our countrymen feel we have done a useful bit of work we shall be amply rewarded for what has been a very difficult and most strenuous month.

Society of Incorporated Accountants and Auditors.

MEMBERSHIP.

The following promotions in, and additions to, the Membership of the Society have been completed since our last issue:—

ASSOCIATES TO FELLOWS.

CARR, GEOFFREY (Muir, Moody & Co.), 20, Newgate Street, London, E.C.1, Practising Accountant.

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THE INDEPENDENCE OF AUDITORS.

To the Editors *Incorporated Accountants' Journal.*

SIRS,—I would like to refer to the very able article which appeared in *The Statist* of August 6th last on "The Independence of Auditors." The writer comments upon the division of professional opinion regarding the necessity for amendment of company law with a view to defining and clarifying the duties of auditors, and points out the reluctance of auditors to maintain views which derive no legal support from the Companies Act. This latter consideration is a strong argument against those members of the profession who maintain that it can be left to the profession itself in practice to bring about reforms, for the reason that in cases where auditors' views may be in conflict with those of directors, the auditors' power is almost invariably limited by the provisions of the Act.

The article, however, mainly deals with the unsatisfactory provisions of the Act with regard to holding and subsidiary companies, and especially so far as regards information required to be furnished regarding subsidiary companies with which the auditor has primarily no concern nor responsibility. The writer emphasises how important it is that shareholders should be given information as to the earning capacity of their company and indicates various methods which might be adopted to ensure this result. The circumstances vary so greatly in different cases, however, that it is impossible to lay down that any special method should be adopted, but I maintain that unless the results of the operations of subsidiary and sub-subsidiary companies are incorporated in the profit and loss account of the holding company then the extent to which such results have not been taken into account should be clearly shown on the face of the published accounts. This was one of the recommendations contained in the Report of the Council of the Society on Company Law and Accounts. With the law as it stands at present the accounts of holding companies may be quite misleading as to the true result of its operations. In this connection the writer of the article says :—

> "Until some such reform either of the law or accountancy practice is brought about it will not be possible to assume with any confidence that the accounts of large concerns do really show the true state of affairs, and if the accountancy profession can hasten progress along these lines, with or without legal support, it will deserve the gratitude of the whole commercial community."

This consideration does not apply only to large concerns, but to every company having one or more subsidiaries, whose results are not incorporated or not disclosed in the accounts of the holding company.

I contend that without legal support the accountancy profession can do little to remedy the present unsatisfactory practice in dealing with the results of subsidiary companies.

May I suggest that the article I refer to might be published in your next issue of the *Journal*?

Yours faithfully,

HENRY MORGAN.

London.
August, 1932.

[The article referred to appears in another column.—EDS., *I.A.J.*]

Liabilities of Administrative Officers of Limited Companies.

A LECTURE delivered to the Incorporated Accountants' District Society of Liverpool by

MR. BERTRAM B. BENAS, B.A., LL.B.,
Barrister at-Law.

MR. BENAS said: In a memorable phrase, Sir Henry Maine, in his classic volume entitled "Ancient Law," observed that the movement of progressive societies has been from status to contract. Like all epigrams, the condensation of language, while helpful in summing up a full consideration of the subject, does not always assist elucidation at first acquaintance. Transcribing Sir Henry Maine's phrase from verbal shorthand to verbal longhand, if one may be allowed this mixed metaphor, the point which the learned jurist sought to establish is that the further back we go into the history of the community we appear to deal with groups of persons who possess rights and duties as members of the group, because the *group* earmarks (in early days very literally) the position of the individual in relation to the community as a whole, rather than to deal with the *individual* possessing rights and duties as such, independently of any other group but the community as a whole. We see in various ways later developments of that idea in the London City Guilds, somewhat earlier the various grades of the rural community, such as the yeoman farmer and the so-called serf, and we gradually see this group consciousness fading into a perfect blaze of individualism in which the individual, *qua* individual, alone is counted. During the second half of the last century the wheel has shown signs of coming full circle, and trade unionism, employers' combinations, and the enormous growth of joint stock companies have all tended towards this end, to say nothing of the evolution of political ideas which in every party of the State has shown a direction away from unrestricted individualism. These observations are preliminary to my statement that the accountant, in considering his legal position, cannot wrap himself in the mantle of any historic group consciousness which would endow him with a special set of liabilities or immunities at Common Law. If my reading is correct, his Guild is not really old enough to have claimed by antiquity any such privileges and Equity which in Maitland's brilliant phrase "Came to fulfil and not to destroy the Law," while it placed, or rather its books placed, in a special category "the taking of accounts" never made the accountant a special class for itself as the special object of its attentions such as it did with infants, married women and lunatics. So the accountant is neither above nor beneath the Law, but just naturally poised on its level. True, statute law, which often enough upsets all calculations, shows signs which illustrate my statement as to the movement of the wheel, and particularly in company legislation of recent date we begin to detect the definition of what one might call group liabilities in respect of accountants.

But, speaking generally, the accountant must rest content that he has no exemption from the maxim that "Ignorance of the law is no excuse," and that he can search the Statute Book from beginning to end and will find no Statute entitled "The Law of Accountancy Consolidation Act." To know his rights and duties he must piece together those elements of the law which concern his functions and liabilities. If I were asked to state what branch of the Common Law an accountant and a secretary should be conversant with, in the first place I should unhesitatingly say the Law of Contract. This

is fundamental to a knowledge of the legal basis of every business transaction. It is almost impossible to conceive a single transaction of any person in the normal course of a normal day which does not involve the application of the Law of Contract, but the process, like that of the motion of the earth when normal, is so regular that we are quite unconscious of the proceeding taking place. Some principles of the law have in text books become grouped together under the title of "Commercial Law or Mercantile Law," and something like authority has been given to the description by the reservation of one of the Courts of the King's Bench Division for the disposal of work dealing with the subject usually grouped under that title. It will, however, remain to me always a puzzle why the law relating to Land should be regarded as outside Commercial Law for the purposes of study by non-legal professional men, although, of course, as a Chancery barrister I quite appreciate why legal business relating thereto should not be decided in the Commercial Court. Therefore, the accountant and secretary, after having dealt with the Law of Contract in general, should make himself familiar with what are largely statutory codifications or consolidations of the Common Law, such as the law relating to Bills of Exchange and Negotiable Instruments generally and Insurance and Shipping, while two subjects which Statute Law has developed out of both Equity and Common Law, namely the law of Partnership with its great descendant Company Law (according to the view of the late Lord Lindley) and Bankruptcy Law are essential topics the accountant and secretary must be familiar with in every sphere of practice.

Of recent years enormous developments in the practice of accountants have taken place in relation to the Inland Revenue, and this work involves a knowledge of the law and practice of taxation both for the purposes of Inland Revenue and Local Revenue, while if the secretary is not so much concerned to know the law in relation thereto he will find it necessary to have a good working acquaintance with its practice. The secretary, on the other hand, quite obviously realises the need for a complete grasp of company legislation, while the accountant has to bear in mind that company legislation has for him great demands not only on his knowledge but upon his vigilance, since the Finance Acts and the company legislation get often interlocked. In my opinion there are some special subjects of Equity which call for the attention of both the accountant and the secretary, and they are, in particular the chapters on accounts in the equity textbooks and those relating to Trusts, the Administration of the Estates of deceased persons, Mortgages, and the remedial processes which Equity provides, namely, Receivers and Managers, and Equitable Execution generally. The accountants take their place as a statutory category when they become auditors to a company, and of the other statutory offices of the company which have become categorised there remains to be dealt with later, the director and the secretary. The auditor, the director and the secretary afford further illustrations of the movement of the wheel which I referred to at the beginning of my paper.

The first business of an auditor is to be familiar with the Articles of the company relating to his special duties. This was the gist of the judgment of Lord Justice Lindley (as he then was) in *Re Kingston Cotton Mills Company* (1896, 2 Ch., 279). He must certify to the shareholders as to the true financial position of the company. I recommend for reading in respect to this duty another judgment of Lord Justice Lindley (as he then was) entitled *Re London and General Bank* (1895, 2 Ch., 673). It is in the very nature of things that auditors must have recourse to the representations of the officers of a company, and they will not be liable for difficulties arising therefrom if they take reasonable care. Lord Justice Lopes in *Re Kingston Cotton Mills Company* (1896, 2 Ch., 288) observed "that an auditor is justified in believing tried servants of the company in whom confidence is placed by the company." He is entitled to assume they are honest and to rely upon their representations, provided he takes reasonable care. If there is anything calculated to excite suspicion he should probe it to the bottom, but in the absence of anything of that kind he is only bound to be reasonably cautious and careful. It follows, therefore, that if there is no cause to excite suspicion, reasonable inquiries should suffice. Where expert opinion is submitted dealing with some matter the auditor is entitled to rely thereon (see *The Leeds Estate Building Society* v. *Shepherd* (36 Ch. D., 787)). This, of course, does not mean that an auditor can depute to others the examination of that which it is his function to examine personally. The most recent authority on this point is in *Re The City Equitable Fire Insurance Company* (1925, Ch., 407), where, at page 497, Mr. Justice Romer (as he then was) dealt with the question of custom in relation to auditors. By sect. 152 of the Companies Act, 1929, any provision in the Articles or in any contract with the company or otherwise exempting an auditor from or indemnifying him against liability which by any rule of law would otherwise attach to him in respect of any negligence, default, breach of duty or breach of trust is void. An auditor, however, can be relieved by the Court under sect. 372 of the Act if the Court is of opinion that he has acted honestly and reasonably and having regard to all the circumstances of the case, including those connected with his appointment, ought to be excused. In general, auditors are entitled to have access to the books of the company, but there are circumstances under which such access may be, at all events for a time, withheld, as when there is a dispute between the auditors and the company, as in the case of *Cuff* v. *The London and County Land Company* (1912, 1 Ch., 440). Auditors must check the statements in the balance sheet as to the amount of capital, at the bank and in hand, by looking at the pass book or obtaining a certificate from the bank. See *Fox & Son* v. *Morrish Grant & Co.* (35 T.L.R., 126).

As far as my reading goes, I have never come across any case which deals with the accountant as such in any other way than under the general category of a professional person holding himself out as one duly equipped to carry out the exercise of his calling. If I were to state that that involved two propositions, one that he must act reasonably, and its correlative, that he must not act negligently, I do not seem to be telling you very much, but in point of fact I am telling you all that the cases dealing with the liability of professional persons virtually amount to. The traditions of a profession form safe guides for what has to be avoided to be other than negligent, and common sense and character are sure foundations upon which to base that which is reasonable. Both essentials, the exercise of reasonableness and the avoidance of negligence, point to the prime necessity of personal training in addition to learning from books.

I am bound to add that I consider the general neglect of the study of subjects studied together as a group under the title of Equity in our schools of commercial training are often the cause of a good deal of trouble into which the secretary and accountant sometimes fall. Commercial Law is usually studied from a Common Law angle of vision, and Common Law fastens upon the idea of negligence and the idea of deceit in more obvious cases than obtains in Equity.

The Equity mind has a kind of detective tendency to

scent Breach of Trust, Fraud and Misrepresentation when the tracks of these wrongs have been covered up, and engenders in the mind of those who are indoctrinated in its principles a belief that while everything may be above board it is sometimes useful, and very often necessary, to pull up the boards and see if there are not smouldering fires. My metaphors may be mixed, but I hope not my meaning.

When I turn to the secretary I come to a person whom the modern practice of commercial life has saddled with as many duties, and of as many different kinds, as the Legislature has saddled the County Court bench.

He has to be conversant with accounts, but is not the accountant nor the auditor. He has to be conversant with the law, but is not the solicitor to the company or, more accurately, the solicitor in respect of any of the points upon which he happens to be laying down the law. He has to manage generally, but he is not the general manager. Very often he has to direct, but he is not a director, and he may often find himself taking the chair, metaphorically speaking, without being the chairman. No wonder, then, that so many young people anxious to get on in the world and secure a comfortable position are anxious to qualify as secretaries! If the secretary does that which is right in the several spheres with which he is concerned the matter usually finds its way into the special department concerned, and those in charge thereof get properly thanked. If, however, the secretary is wrong he will be blamed as being incorrect in what he has done, which from another point of view is also right. So that, as I have mentioned before, the lot of a secretary, like that of a policeman, is altogether a happy one! We may group the various secretarial functions as follows :—

1. Those relating to the law. He must be a kind of legal handyman, having a particular eye to the statutes relating to the special business of the company in addition to the general Company legislation, the Revenue legislation, and at least so far as land law is concerned the law of Landlord and Tenant.

2. Those relating to his functions as a registrar. He must supervise the application and allotment of shares, the certification and registration of transfers, probates and other administration documents, and dividend transmission.

3. The organisation of meetings. He must arrange the various meetings, issue the notices convening them, settle the agenda, record the minutes, and see that the resolutions are duly carried into effect.

4. Those relating to finance. Here his functions may be very various, and these will largely depend upon the nature and dimensions of the company, but in any event he must keep a vigilant eye upon the exercise of borrowing powers, raising of new capital, the accounts, the audit and the issue thereof, and the state of investments.

5. Under the heading "general" must be grouped all those functions not included in the previous groups, and they comprise that of keeping the statistics of the company, attending and filing the correspondence, insurance, rating, and all those additional matters which require attention for the due running of the machine as a whole.

Having given a general description of the spheres of accountant, auditor and secretary, let me deal a little more particularly with accounts and audit as viewed in the light of the Companies Act, 1929. It is, of course, impossible within the time and space at my disposal to do more than point to the important changes which the new Act introduced, making proper accounts a statutory obligation. Under sect. 122 the obligation is imposed upon every company to cause proper books of account to be kept with regard to :—

(1) Moneys received and expended.
(2) Sales and purchases of goods.
(3) Assets and liabilities of the company.

Failure to cause this to be done imposes serious penalties upon the directors. Sect. 123 imposes upon directors the obligation to prepare and lay before the company in general meeting not later than 18 months after incorporation and subsequently at least once in every calendar year a profit and loss account.

Special provision is made for companies with interests abroad and for a grant of extension of time by the Board of Trade.

A balance sheet must be made up to the same date as the profit and loss account, as well as a report in every calendar year.

Similar penalties for failure to comply with these requirements are imposed upon directors.

Sect. 124 particularises the requisite contents of the balance sheet. Sects. 126, 127 and 128 are vitally important with respect to holding companies and subsidiary companies.

Companies whose assets consist of shares in subsidiary companies must set them out separately from all other assets, and the aggregate amount of indebtedness must be set out separately from all the company's other liabilities. There must be annexed to the balance sheet of the holding company a statement stating how the profits and losses of the subsidiary or subsidiaries have been dealt with for the purposes of the accounts of the holding company, and reference should be made to the sections for many other special requirements. Sect. 127 defines a "subsidiary company."

Loans to, and remunerations of, directors must be disclosed in the accounts. Sect. 129 lays it down that the balance sheet and statement, the latter in the case of a holding company, must be signed by two directors or by a sole director, and the auditor's report must be attached. A penalty up to £50 is imposed for failure to comply. The auditor's report must be read before the company in general meeting, and must be open to inspection by any member. Except in the case of a private company, all persons entitled to receive notices of general meeting must have sent to them seven days before the date of the meeting copies of the balance sheet, including every document required by law to be annexed thereto, and the auditor's report. Failure to comply involves a penalty up to £20. Any member or debenture holder not otherwise entitled may demand a copy of the last balance sheet and auditor's report. Failure to comply involves a penalty of £5 per day of default. In the case of a private company any member may require the company to furnish within seven days a copy of the balance sheet and auditor's report at a charge not exceeding sixpence per 100 words. Failure to comply involves a default fine. These provisions are contained in sect. 130 of the Act.

Sects. 132, 133 and 134 deal with the auditors rather than the audit. Sect. 132 requires the auditors to be appointed at each annual general meeting to hold office until the next. If not so made, the Board of Trade may appoint the auditors and fix their remuneration. Only the retiring auditors can be appointed unless notice has been given fourteen days before the annual general meeting. The first auditors are appointed by the directors until the first annual general meeting. The directors may fill casual vacancies.

The remuneration of auditors who have been appointed either before the first annual general meeting or to fill casual vacancies is fixed by the directors. In all other

cases, except where made by the Board of Trade, the remuneration is fixed by the company. Sect. 133 disqualifies for appointment as auditor: (1) Directors or officers of the company; (2) except in the case of a private company, a person who is a partner or employee of an officer of the company; (3) a body corporate unless acting under an appointment made before August 3rd, 1928, Subject to the last mentioned proviso, a body corporate which acts as auditor of a company shall be liable to a fine not exceeding £100. Sect. 134 makes statutory a report by the auditor. Auditors must have access to the books and accounts and vouchers of the company, and are entitled to require all information and explanation from the directors and officers of the company as may be necessary for the performance of the duties of an auditor. Auditors have now the right to attend the annual general meeting and to make any statement or explanation with respect to the accounts. It is worth while to note sect. 365 of the Act, which contains general provisions as to offences: (1) Where by any enactment in this Act it is provided that a company and every officer of the company who is in default shall be liable to a default fine, the company and every such officer shall for every day during which the default, refusal or contravention continues, be liable to a fine not exceeding such amount as is specified in the said enactment, or, if the amount of the fine is not so specified, to a fine not exceeding £5; (2) for the purpose of any enactment in this Act which provides that an officer of a company who is in default shall be liable to a fine or penalty, the expression "officer who is in default" means any director, manager, secretary or other officer of the company, who knowingly and wilfully authorises or permits the default, refusal or contravention mentioned in the enactment.

Let me now deal with some more particularity than hitherto with regard to the legal position of the secretary over and above what I might call the carrying out of the functions which in practice fall upon him to effectuate which in most cases the law imposes upon others to cause to be effectuated. It will be appreciated that it is not possible within the limits of this paper to tabulate a complete set of reminders to the secretary as to the details of the duties which, as a result of the law, he is called upon to discharge in pursuance of obligations imposed upon the directors or the company. The position of a secretary may be generally regarded as legally that of the correlative of master; secretaries are in fact the commercial analogues of civil servants. See *Daimler Company* v. *Continental Tyre Company* (1916, 2 A.C., 307).

The company will only be estopped by his fraud where it was his duty to deal with the matter, and where it was the duty of the secretary to certify transfers when the certificates were left with him the company was held not liable on his certifying a transfer without a certificate being left. The cases of *Whitechurch* v. *Cavanagh* (1902, A.C., 117), and *Lloyd* v. *Grace, Smith & Co.* (1912, A.C., 716) may be usefully consulted on the principles involved. For instance a person who has been induced to take shares in a company by means of a fraudulent misrepresentation of the secretary will have no remedy against the company, see *Partridge* v. *Albert Life Assurance* (1871, 16 S.J., 199). *Prima facie*, a secretary has no authority to bind the company. The dicta in *King's Cross Industrial Dwellings* (1870, 11 Equity, 149) indicating that a secretary has implied authority to bind a company by contracts for preliminary advertising must be taken with reserve, since in that case there was actual authority to do the act. In support of the general principle, the most recent case which is of general use is *Indo-China Steam Navigation Company* (1917, 2 Ch., 100). From, however, the case of *Longman* v. *The Bath Electric Tramways* (1905, 1 Ch., 645) it appears that a company would be liable for the negligence of the secretary in the ordinary course of his duty. Turning from the Common Law liabilities to those more in the sphere of Equity, it may be stated that, speaking generally, the position of a secretary would *prima facie* not be regarded as a fiduciary one. The cases of the *Municipal Freehold Land Company* v. *Pollington* (53 L.T., 238) and *Martinsen* v. *Clowes* (21 Ch.D., 857) may be usefully consulted hereon. In the latter case it was held that he may not bid on an auction of the company's property where he has instructed the auctioneer himself. This, however, does not fasten upon the secretary generally all the immense weight of obligations which Equity places upon the shoulders of those whom it endows with a fiduciary position. In general he will not be liable for the acts of the board of directors unless he has in some way identified himself therewith over and above the normal function of a secretary. The case of the *Municipal Freehold Land Company* v. *Pollington*, which I previously cited, may be usefully considered on this point, as also *ex parte James* (49 L.T., 530). Sect. 17 of the Stamp Act, 1891, involves him in a penalty of £10 for failure to enrol, register or record not properly stamped. Sect. 113 of the Companies Act, 1929, enacts that the name and address of the secretary must be set out in a statutory report which sect. 113 requires. He is liable to penalties for failing to make various returns, for which see in particular sects. 42, 80, 81 and 91, but its seems that he is not liable for the penalty for default in calling an annual general meeting. Under sect. 129 he must sign the balance sheet of a banking company and, if duly authorised, authenticate documents under sect. 33. Where a person acts as secretary to two companies, the mere existence of the common relationship does not involve the principle that a fact which comes to his knowledge as secretary of one company is notice to him as secretary to the other company. In order to constitute notice it must be shown that it was his duty to the first company to communicate his knowledge to the second company. See *Fenwick, Stobart & Co.* (1902, 1 Ch., 507). A secretary is liable to severe punishment for falsification by him of any books or documents of the company. Sect. 272.

It would seem that the incompatibility of the office of director and secretary are such that the same person cannot hold both offices.

This is probably a consequence of the working out of the common law doctrine of service. A secretary is liable for misfeasance if he receives an improper commission. See *McKay's* case (2 Ch.D., 1). He cannot be personally liable for a mis-application of the company's funds other than by himself though he may have known all about it. See *Joint Stock Discount Company* v. *Brown* (1869, 8 Equity, 396).

The above represents some of the main principles of the law as applied to secretaries. While the legal training of an accountant and a secretary should be largely on the same lines, I am convinced that some knowledge of the principles of the Law of Torts—that is to say, wrongs independent of contract—is very needful for the secretary. It is one of the curiously interesting features of company law that its very comprehensiveness causes one to step almost in a moment from the realm of Common Law and Equity into the territory of the Criminal Law. I do not think that even the outline of Criminal Law is a necessary subject either for the secretary or for the accountant, as the branches of the Criminal Law involved are sufficiently specific to be able to be noted at the points required, nor is there any special doctrine as in the civil sphere of the

Common Law which it is necessary to understand before being able to accept the statements of the criminal law on the particular points as they are found; but, like the man who did not realise he was speaking prose all the time, the secretary is constantly observing Contracts and avoiding Torts at every moment of the day, almost unconsciously.

I neither think it possible nor strictly appropriate in this place to deal with the position of directors. They are, perhaps, hardly administrative officers of a company within the more limited meaning that the scope of my paper envisages.

Their duties and liabilities are heavy enough to warrant separate treatment. I would, however, like to conclude with an optimistic note. While I would most strongly urge secretaries and accountants to read and ponder over the troublesome cases involving company law which created so great a sensation during the last few years, I would beg of them not to allow these cases to convert caution into fear or vigilance into anxiety. The number of wrecks, after all, largely emphasises the safety of navigation, and the good ship "Company" can confidently look forward to many a safe voyage guided by trustworthy captains and faithful crews.

Changes and Removals.

Mr. A. W. Bond has taken into partnership Mr. H. A. Morley. They will practise at 99A, High Road, Beeston, Nottingham, under the style of Bond & Morley, Incorporated Accountants.

Mr. E. E. Edwards, Incorporated Accountant, announces a change of address to Bank Buildings, Aberdare.

Mr. Jack Hoffman, Incorporated Accountant, has removed his offices to Fletcher's Chambers, Darling Street, Cape Town.

Messrs. Johnstone, Davies & Moulder, Incorporated Accountants, 13, Church Street, Kidderminster, announce that as from September 1st the partners in the firm will be Mr. William Johnstone, Mr. Harry Moulder, Mr. W. N. Tranter and Mr. G. A. Tyers. They will practise under the style of Johnstone, Moulder & Co., Incorporated Accountants. Mr. O. W. Davies has retired from the firm and has entered into partnership with Mr. W. A. Mumford. They will practise at Market Chambers, High Street, Kidderminster, under the style of O. W. Davies, Mumford & Co., Incorporated Accountants.

Miss R. G. Kendall, Incorporated Accountant, has commenced public practice at Capel House, 54, New Broad Street, London, E.C.2, in partnership with Mr. A. J. Field. They will practise under the firm name of Kendall & Field.

Messrs. Saxton, Shaw & Co., Incorporated Accountants, have admitted into partnership Mr. J. K. Brown, A.S.A.A. The practice will be carried on in future under the style of Saxton, Shaw, Brown & Co., at new offices at 14, Regent Street, Barnsley.

Messrs. H. Theobald & Co., Incorporated Accountants, have removed their offices to 15, Farringdon Avenue, London, E.C.4.

Mr. P. E. T. Whiteley, Mr. L. A. Whiteley, and Mr. R. B. Hogg, practising as Whiteley Bros. at Beresford House, Main Street, Johannesburg, have retired from the firm of Gibson, Whiteley & Co., Incorporated Accountants, Cape Town. Mr. C. D. Gibson and Mr. Hugh Hyslop will continue to practise under the same style and title at Namaqua House, Cape Town.

CONSPIRACY ALLEGATIONS AGAINST DIRECTORS AND AUDITOR.

Judgment on Appeal.

The following is the judgment of the Court of Appeal in the case of the *Combined Pulp and Paper Mills, Limited.* Last month we published the speeches of Counsel and the fact that (just as we were going to press) the appeals had been dismissed.

Lord Justice Scrutton, giving judgment, said the case took twelve days to try, before Mr. Justice MacKinnon and a special jury, and the appeal lasted twelve days. Even at the risk of omitting to deal with some of the points argued, the Court had decided to give judgment before the Vacation.

The Court had come to a unanimous conclusion on all matters argued before it.

The time occupied by the case was not excessive. In the course of three years, nearly a million of shareholders' money had been lost. It was most desirable that such a disastrous result should be fully investigated. There were various allegations made against the defendants in the case, but by the end of the trial before Mr. Justice MacKinnon the main issue on which the parties were fighting was honesty or dishonesty: Were the acts complained of honest or dishonest? The Judge reported that in his opinion the jury which sat with him to try the case was an exceptionally good jury. Its foreman was a Chartered Accountant, and there were two other Chartered Accountants on it. There was no lady on the jury, and that was an advantage where heavy business transactions had to be considered. The documents they asked for were very material documents, and the jury showed very great intelligence in grasping the business problems presented to them.

After retiring, the jury sent a communication to the Judge. Mr. Justice MacKinnon was tired after a day and a-half of summing up, and he momentarily forgot that that communication and the Judge's reply should be made public at once, so that Counsel might express their views on the reply to be given.

After the verdict, Sir Patrick Hastings asked that the jury be invited to say whether they found on the ground of fraud or wilful default. The defendants did not support that application. I daresay, said Lord Justice Scrutton, they exercised a very wise discretion in not asking, but having exercised that discretion it is too late now for them to say there is no verdict. The objection to the verdict on the ground that it did not find whether the defendants had been guilty of fraud or wilful default failed. The result was that there was a general verdict. If there was evidence to support it on any of the matters in issue, there was no remedy in the Court of Appeal.

Was there evidence which would support the verdict on the ground of either fraud or wilful default, and was there any misdirection? The fact that conspiracy dropped out of the Judge's summing up was very much in favour of the defendants. No valid objection to the summing up could be taken on the ground that the case was not put as unfavourably as it might have been.

The matter of wilful default was more troublesome. It would not trouble the Court in future because the Companies Act, 1929, said that an Article exempting directors from the consequence of negligence or wilful default would be void. It was contrary to public policy. Consequently, the Courts would not in future be troubled with the question of what constituted wilful default. It

was notable that all past cases in which this question of wilful default was raised started with an admission of honesty. If there had been an admission of honesty in this case, a much more detailed direction with regard to the duties of directors and auditors would have been required, but no such careful direction was needed where the question was whether the director or auditor had been honest. For that reason, one of the main objections to the summing up failed owing to the course taken by the case.

Was there evidence to support the verdict on the ground of fraud or wilful default? His Lordship agreed with the Judge that where fraud was alleged, wilful default was practically the same as fraud. There was evidence, continued Lord Justice Scrutton, on which the jury could find that Philipp and Spier, the vendor and promoter, knew that Koslin (a subsidiary) was an unprofitable company, that they represented it as a profitable company, provided it with a board that was not really independent, and by payments made or allowed to be made to individual members created such a condition of mind in the directors and auditors that they were ready to support and take part in any schemes put forward by Philipp and Spier, however fantastic and void of foundation they were.

There was evidence on which the jury might find that an unjustifiable dividend, supported by fictitious documents, was declared by the directors and sanctioned by a general meeting of the company—induced to do so by two speeches of Oppenheimer—and that this action was taken to obtain capital which would be used for the benefit of Philipp and Spier in ridiculous schemes, in the manipulation of schemes which Philipp had created. In other words, there was evidence on which the jury could find that all the defendants put forward a delusive and unreal balance sheet (either knowing it to be untrue or reckless about it) in order to justify a dividend not represented by profits, but to be used for supporting a further issue of capital to bring profits for Philipp and Spier and their associates.

Bruno Philipp's first object was somehow or other to manufacture a balance sheet for the Combined Pulp which would justify a dividend of 20 per cent., and enable the company to make a new issue of capital. In that issue there would be heavy commissions for underwriting. It was essential to secure that object that there should be put forward some objects on which the new capital would be expended when obtained. It is really difficult, said Lord Justice Scrutton, to state gravely the extraordinary proposals which were put forward by Philipp. They look so ridiculous that it is difficult to believe any sane people would ever believe in them. It looks more like the Mad Hatter's tea-party in "Alice in Wonderland," and it would be an interesting speculation to see who was to take the part of the Mad Hatter, and who was to take the part of the dormouse. Most of the proceeds of the new issue were to go, and did go, to Bruno Philipp by means of the company juggle.

In justice to the individuals, it was only fair to state why the jury might have found against them. Sir Walter Townley's case was a melancholy one. He is one of a class of people who are one of the difficulties of company business in England. Judges are fortunately free from the temptation, because they have no retiring age, but in other professions—diplomacy, the Army, the Navy—there comes an early retiring age, and a man finds himself with a small pension at a time when he thinks, and properly thinks, he is competent to go on doing work. He has an honoured name with the public, and that is what the company promoter wants. The company promoter wants a man whose name will appeal to the public, and who does not know too much about business. The name will attract capital. The company promoter will manage the rest. Sir Walter Townley said to the jury in his evidence: "I don't know much about accounts." He said to us in his speech: "I don't know anything about law," and he also said there were other apparently able people who appeared to understand the matter, and he was a passenger. He was a paid passenger. Promoters might get him to do things that very likely he did not completely understand, but which he never took the trouble to understand. There was evidence on which the jury could hold that he was reckless.

With regard to Mr. Goldsmith, he signed the cheques of the company. For some reason, the company did not receive a report of cheques signed, and there was evidence on which the jury could find against him in respect of these. From letters written by Spier to Bruno Philipp, it was plain that the two were acting in their own interests, and not in the interests of the company. Philipp himself was past praying for.

The cases of Oppenheimer and Froude had given the Court great difficulty. In Mr. Oppenheimer's favour was the fact that he was at times very critical of Mr. Philipp. He took action which, if persisted in, might have entirely destroyed Philipp's plans. Unfortunately, it was not persisted in. What the Court would have done had it been the tribunal to judge, he (the Lord Justice) did not know. There was no ground for interfering with the verdict.

As to Froude, if this had been a case of negligence only there would have been need for much more careful directions as to the duties of auditors, but from the series of trial balance sheets he drew up the jury might easily have drawn the inference that what he was trying to do was to get a gross profit of £200,000, and get it in all sorts of different ways. It could not be said that there was no evidence on which the jury could find against him either on the ground of fraud or wilful default.

Lords Justices Lawrence and Greer concurred.

Mr. Cyril Atkinson asked that the judgment against Mr. Froude be corrected by reducing it by £738.

Lord Justice Scrutton: Yes.

Mr. Pritt: Does the judgment stand in form that plaintiffs are entitled to recover £92,400 from each of the others?

Lord Justice Scrutton: In form, yes. I don't think it will make any difference.

Sir Patrick Hastings: I ask that the appeals be dismissed with costs.

Lord Justice Scrutton: Yes.

Incorporated Accountants' Golfing Society.

The autumn meeting of the society will be held at Coombe Hill Golf Club, Kingston Hill, Surrey, on September 29th.

A Medal Competition will take place in the morning and four ball matches will be arranged in the afternoon.

It is hoped there will be a large attendance of members and guests, who may be introduced by members of the society.

Mr. N. J. Shah, Incorporated Accountant, has been elected to the Senate of the Bombay University from the Registered Graduates' Constituency. His term of office as a Fellow of the University will be for five years.

Investigations.

A LECTURE delivered to the members of the Incorporated Accountants' Bradford and District Society by

Mr. ARTHUR B. THOSEBY, A.C.A.

Mr. THOSEBY said: At the outset I wish to make a few general remarks about the subject and its increasing importance from the standpoint of our profession. During recent years you cannot fail to have noticed the rapid growth of the idea that the accountant is to be regarded as the "commercial adviser, analyst and doctor." Even the public is now educated to the idea that an accountant is the fit and proper person to investigate anything "commercial." I am of the opinion that this view must continue to extend, and that those members of our profession who set themselves to meet the demand for specialised service of this description will benefit accordingly. This is an analytical and inquiring age as well as a strenuous and competitive one, and I believe our profession has a definite and important part to take on the lines I have indicated.

Apart altogether from this, I can commend such work to you from the standpoint of general interest. No one could truthfully refer to our profession as constituting a continuous round of excitement, but it is perhaps closest to excitement on investigation work, for this reason: there you are compelled to study people and their actions as well as facts and figures. On investigation work you can regard yourselves as commercial detectives. Most of us have a strain of the detective in us, witness the public demand in these days for that type of fiction. In this connection, some few weeks ago I happened to notice a reviewer's comments on a book by one of our leading writers of detective fiction where the phrase occurred "has confounded the old adage by making fiction stranger than truth." Well, you may come across some things which are both strange and true whilst engaged on investigation work. I suppose the thrill in detective fiction lies in the totally unanticipated solution. You can get something of the same thrill out of investigation work. For instance, imagine the thrill of being instructed by a client to find out what is the matter with his business, and ultimately discovering it is the client himself. I cannot very well give you personal experiences to-night, but I can promise you great interest and even excitement in this fascinating field, and I hope what I have said may be sufficient to attract some of those present to my subject and to provide the necessary tonic for anyone present who has been spending the day adding up a day book or checking stock sheets.

Every investigation is somewhat different, calling in some part for different treatment, but, of course (as the text books would say), there are general rules subject to modification in certain cases. Having this in mind, you will understand that my lecture must be viewed as indicative rather than particularised.

Our training as accountants and auditors should fit us to make deductions and to draw conclusions from masses of figures which to the uninitiated would seem either confusing or entirely meaningless. An investigating accountant must certainly be able to do this, but, in addition, he must have other qualities: to name a few, tact, reasoning power, some ability in cross-examination, general knowledge (the wider the better), and, above all and vitally necessary, common sense. It is quite true that some people are better endowed by Nature with these gifts than are others, but, to the students present, I would say that some of these qualities can be developed, more particularly reasoning power and general knowledge. I must assume that anyone who can pass the Final examination of the Institute or the Society has a certain amount of the vitally necessary common sense.

Much of what I shall have to say to-night must of necessity deal with the practical side of investigation work, but I do wish to emphasise the fact that in many instances the most valuable information and guidance will not be gleaned from the books nor from a comparison of figures, but rather by the application of the other qualities I have mentioned. From this you will understand that I believe each separate investigation, and the various interested parties, requires careful study, not only with a view to getting at the truth, but to supplement and assess the deductions and conclusions you will make from the books and records, the latter being what may be termed the practical side of the work.

Speaking generally, the investigation work which a practising accountant is called upon to do may be expected to fall under the following headings:—

On behalf of a client who is wondering whether to purchase or invest money in a business.

On behalf of a client (shareholder, proprietor or creditor) having money in a business and wondering how to get it out, or, alternatively, what to do with the business. (Generally you have to find out why the business is losing money and whether it can be made profitable.)

The detection of fraud. This heading includes fraud arising in connection with taxation where an investigation is undertaken with the idea of ascertaining the nature and extent of undisclosed liabilities for taxation.

I am going to deal with the last heading first, and as briefly as possible.

The detection of frauds of the "cashier type" usually necessitates reconstruction of the books, generally effected by obtaining copies of ledger accounts from suppliers and customers, and copies of the bank pass books. Frauds arising by way of stock leakage can only be proved if the records permit of the preparation of what is tantamount to a Material or Stock Account. The type of business, as well as the adequacy of the records, must be carefully considered before embarking upon such work, otherwise you may find, after your labour, that the results are incomplete or unconvincing. Whilst on this subject, I would like to say that I take the view that practising accountants should indicate to their clients the advisability of maintaining in their businesses adequate material and stock records permitting either an internal or professional audit of quantities and production. In some businesses stock leakage would thereby be eliminated; in many businesses, valuable data on production, as well as other "up to the minute" information, would be the reward for the effort and expense. At this point may I venture a word of criticism on my own profession? As professional auditors, I believe we spend too much time verifying the petty cash, whilst leaving the stock (quantities and valuation) severely alone, this although the stock probably represents the major part of the liquid assets of the business. However, I must not digress from my subject.

Fraud in balance sheets and accounts should not occur where reputable auditors are employed, but the fact remains that fraudulent, wilfully misleading and unduly optimistic balance sheets, have been known to exist and to require exposure. The work in such a case will usually call for a re-audit of the books, probably coupled with re-assessment and careful verification of the

assets and liabilities. In passing, I may say that in such a case the stock is usually found to be inflated in value or even non-existent. Much of what I shall have to say later bears upon the subject of the re-assessment and verification of a balance sheet, and is equally applicable to this type of fraud.

Taxation investigation work is usually undertaken under the guidance of the Inland Revenue Authorities themselves, and therefore I do not propose to discuss it at length. I may say, however, that taxation frauds take many forms, the omission of sales, the duplication of purchases, omission and undervaluation of stocks, fictitious and improper expenses, and, in the case of private individuals, omission of income. The work usually calls for the reconstruction of the books, the examination of expenses, sometimes for the preparation of Material or Stock Accounts. In the case of an individual, the work often centres round a close examination of private bank pass books, and the attempt to discover where all the assets have come from. Here you encounter what is known as the " means test." This is a method of proving, in a general way, whether all income has been accounted for. You start with the individual's assets on a certain date (say the commencement of a year), add his known income and any legacies or gifts, deduct a reasonable sum for living and known expenses, and thus arrive at his approximate wealth at the end of the year or longer period. If his actual wealth at the end of the year or period shows a higher figure the inference is that some source of income remains undisclosed. Ingenuity and patience are essential qualities for this type of work.

I shall now turn to the other two classes of investigation work, which are more likely to interest my listeners since they are more often encountered. You will no doubt remember my definition of the two classes :—

> On behalf of a client who is wondering whether to purchase or invest money in a business.
>
> On behalf of a client (shareholder, proprietor or creditor) having money in a business and wondering how to get it out, or, alternatively, what to do with the business.

At this point I will mention four general rules of procedure which are almost universal in their application and utility to these two classes of investigations :—

(1) At the commencement of an investigation always try to get someone to show you over the works or place of business and to explain the processes or whatever is done.

(2) Always be a willing listener to anyone in authority who will talk to you.

(3) Do not be afraid of asking questions but do not answer them ; sometimes a particularly innocuous question leads to surprisingly good results.

(4) Keep an open mind and do not commit yourself in the early days of the investigation to any definite view or belief.

The basic principles upon which you conduct your inquiry need not be radically different in either class of investigation and I can conveniently deal with them together. However, I should perhaps point out that the solution to problems of the first class (whether your client shall invest or not) is usually much simpler than the solution to the problem when your client's money is already in the melting pot. In cases of the first class, where there is nothing to hide, you are generally received with open arms, and in any case your duty is simply to advise your client either " yes " or " no " with facts and reasons for your advice. If there is any apparent attempt to limit the scope of your inquiry, or you are not entirely satisfied with the *bona fides* of the party whose business you are investigating, and the degree of assistance he accords, you should advise your client to pass by the investment. In the second class of case, however, you will often experience a degree of resistance from some of the interested people, and even when you have found the answer to the problem you may have to work out all the details of a scheme to meet the situation.

It is almost safe to assume in these days that audited accounts will be available for the business you are called upon to investigate. On receiving your instructions you should call for copies of such accounts (half-yearly accounts if available) covering, where possible, the past four to six years. Having obtained the required accounts, I advise columnar tabulation for purposes of comparison. Alternatively, you may make a careful and comparative visual examination. In either case, the trading account (section by section), the profit and loss account, and the balance sheet should be taken as separate studies. There is an old saying that " comparisons are odious," but they are very useful to an investigating accountant.

It is perhaps hardly necessary for me to remind you that in making some of these comparisons regard must be had and proper allowance made for any known outside factor, such as a noticeable rise or fall in the price of the raw material (or its equivalent) used in the particular business. This may be expressed in another way by saying you must have regard to the purchasing power of the Pound in reference to the particular business under consideration during the period covered by the accounts. Considerations of this nature arise in making a comparison of such items as stocks, purchases, sales and expenses. During recent years the purchasing power of the Pound, expressed in various raw materials and in services, has varied to such an extent that when making a comparison of such an item as sales it has been necessary to compare the physical turnover as distinct from value. To my mind there are certain comparisons, such as sales, which it is always better to base upon the physical figures where available rather than on values.

I am going to assume that due weight has been given to such outside factors, and I shall now proceed to deal with some of the deductions to be made from the careful comparison I have suggested. Firstly, from a comparison of some of the items appearing in what is generally called the first section of the trading account :—

STOCK.

Unless the turnover has risen considerably, even a gradual increase in this figure calls for consideration, particularly if coupled with an increase in the percentage of gross profit earned, or if the turnover be diminishing. Several things may be happening. Obsolete and almost unsaleable stock may still be lingering in the stock sheets. By the way, when you go round the works or business premises have a general look at the stock ; sometimes your eyes may tell you something worth knowing. Alternatively, the values may have been gradually inflated, or the basis of valuation may have been varied. If you are suspicious, you will have to examine the stock position very closely, but I will refer to this work later.

PURCHASES.

Comparisons are not of great value here, but whilst on the subject I may say that there are a number of questions arising out of purchases and applicable to most inquiries which you will do well to consider, such as :—Do the management appear to buy intelligently and in the best markets ? How are fluctuations in buying price carried into the selling price ? What is the degree of co-operation between the buying, the production, and the stock and selling organisation ? These, and similar questions, go

right to the heart of any business, the management, and they are particularly important when you are considering the case of a declining business.

SALES.

Movement, or lack of it, in the figures of turnover is worth considering. If an analysis of the sales is available either by individual areas, materials or anything else, it should be studied, comparatively, if possible. You may find, for example, that the sales of one commodity are falling away, or the sales in one market, or you may find that certain agents are not showing results. Careful analysis of this item, by your own staff if necessary, will usually repay the time and labour, either in the case of a declining business or where your investigation is made on behalf of an intending investor.

If the business involves production, you should endeavour to ascertain the average percentage of machinery which has been employed year by year (shorter periods if possible) and what percentage of machinery has to be employed to avoid losses. In some instances you will have to consider this information with regard to the degree of production likely to be attainable in the future.

RETURNS.

The percentage of returns and allowances to turnover is important and any increase in the figures should receive careful attention. If the figures seem excessive, or if there is an increase, you will find it desirable to analyse the item and to try to ascertain the reason. Correspondence files with customers (your own selection) may tell you something important about this feature of the business and throw light upon the quality of the production.

PRODUCTIVE WAGES AND DIRECT ONCOST CHARGES.

If possible these must be compared with something forming a convenient and reliable standard of comparison. Each case varies, and you must look for the most reliable basis for comparison. If there is some system of costing available, as in a manufacturing business, you may be able to find out if the labour cost per unit is increasing or diminishing, which is a useful check upon the efficiency of the management.

EXPENSE ITEMS.

Now for the second section of the trading account :— Your tabular or visual comparison may at once direct special attention to certain items of expense, but it is usually advisable to examine and analyse the various items critically with a view to discovering whether they are reasonable, or afford scope for the "economy axe." You will note the discoveries you make and the economies you think can be made. The items here are not all susceptible to variation in the same way. The items where economy is frequently possible and where extravagance is most likely to be discovered are the following :—

Salaries.—Call for a list of all salaried people with particulars of their duties. Look back for a few years in the salaries book and try to follow their progress and advancement. You will have to try to find out for yourself what is the calibre and ability of the really important people and the reason for their salaries. You will sometimes find there is the least reason behind the largest salaries.

Motor and Travelling Expenses.—These may call for analysis. Try to ascertain who are the expensive people and what results they achieve. Many businesses are very lax in regulating and checking such expenses.

Telephones, Telegrams and Cables.—A comparatively small item but generally susceptible to the "economy axe" on analysis.

Branch Office, Agents and Similar Expenses.—The personnel and expenses of each branch or agency and its results, improving or the reverse, should be considered. Sometimes you may find that a branch office is no longer justified and may be eliminated with considerable saving. Arrangements with agents may sometimes call for revision or new and livelier agents may be required. In most businesses you find agents' and travellers' reports are available. Some of these should be scrutinised.

General or Sundry Expenses.—This item should be examined as it may conceal anything. Small savings are often possible under this heading.

Stores Items.—The nature of the check on the issue of items of stores is often worth inquiring into. Extravagance occurs where there is no supervision.

Rent and Similar Standing Charges.—Where the business is declining, these items must be considered from the standpoint of the possibility of transferring the business to a cheaper location.

The profit and loss account generally contains little useful information beyond the item Directors' Fees. If you are acting for an intending investor or purchaser you will, of course, have regard to the net results and the dividends which have been or could have been paid on the capital employed.

From a general comparison (a detailed comparison is not really necessary here) of the items in the various balance sheets you will form some idea as to the progress or decline of the business during the period under review, and often you may drop across a clue worth following up. I also recommend you to take the various balance sheets and ascertain the amount of liquid capital in the business at the date of each balance sheet. If the business is a progressive and well-managed business and profits have been earned, you ought to find that the liquid position has been strengthened. A comparison of the figures of liquid capital with the turnover achieved may also be useful, particularly if you have to decide whether the volume of the business can be increased without new capital being provided, or, alternatively, the likely and requisite turnover after introducing new capital.

According to the type of case and your instructions, you will have to decide how far you will discuss your findings and views at this point with the directors or proprietors. If you are acting for an intending investor or purchaser it may not be necessary. If, however, you are trying to find out what is the matter with the business, now is the time to seek separate interviews with the various heads and to persuade them to give you their ideas on the business with reasons for its failure or ideas for its future development as the case may be. You will generally find that some of them are very ready to do this. I do not say you must accept their views or ideas, but it is often useful to know their attitude. Naturally you will not tell them very much.

Apart from what you have learned from your comparisons and from your detailed analysis of various expense and other items, having kept your eyes and ears open you should now know something of the business and the personnel of the management. You will have reached decisions as to whether, in your view, the management is active or passive, resourceful or asleep, intelligent or merely normal.

You may now commence what for lack of a better term I will call the verification of the assets and liabilities of the business.

Many things must be looked for, but I will try to give you an outline of the work.

ASSETS.

Land and Buildings.—Analyse the relative accounts appearing in the books to obtain the original cost and the amount of additions and depreciation written off. According to your instructions, consider such questions as: the date and condition of the buildings? their suitability for the purposes of the business? transport and labour facilities? the room available for extensions? possibilities of sale or division? the existence or possibility of obtaining a mortgage or charge on the property? and the likelihood of appreciation or depreciation in the value of the buildings or site?

Plant.—Analyse the relative accounts as in the case of land and buildings, considering such things as the age of the plant, the amount spent on additions, the amount of the expenditure on repairs and renewals, whether the plant is modern and competitive, or is likely to be superseded. Also, try to ascertain whether any of the plant is out of commission for any reason; in other words, is all the plant capable of effective use in the business, and is the plant well balanced?

Stock.—It will generally be found desirable to test or prove the physical accuracy of the stock. Tests or entire verification may be possible from the material records, if adequate. The valuation may be tested in various ways, against purchase invoices, sometimes against sales invoices, sometimes against costings or material records. The method must depend upon the nature of the business and the type of the stock. I regard the verification of the stock (physical and valuation) as of great importance in making an investigation, either to an intending purchaser or when endeavouring to decide whether a business should be continued or closed down. The stock often represents the most important asset and on it depends very largely the accuracy of past trading results and the possibilities of future trading profit. You cannot give too much time and thought to questions affecting the stock, not forgetting its saleability and the amount of old stock carried.

Debtors.—These can usually be verified very quickly. In examining the ledgers regard must be had to the present position as well as to the balance existing at the date of the last audited accounts, this to discover any bad debts which have arisen in the meanwhile or any new and large accounts which have been opened. You will note the type of customer, the number and extent of the unsatisfactory accounts, and the risk of bad debts (not only in the business but in the particular trade). Also, do not forget that an examination of sales ledger accounts can sometimes tell you whether the products of the business are as acceptable to the trade as they were. You may find that good accounts are being closed and that returns and allowances are increasing. Agents' and travellers' returns, if available, and a few correspondence files with customers are sometimes well worth perusing, as I have already mentioned.

LIABILITIES.

Turning now to the liabilities of the business:—Examine the purchase ledger carefully: also the purchase invoices should be looked over for the period from the date of the last audited accounts to see whether any important accruing liabilities were conveniently forgotten or items wrongly included as in stock. It is also advisable to glance over the payments side of the cash book to see if any unusual payments have been made since the date of the last accounts.

Whilst on this subject I may say that you should always consider whether the last accounts have been prepared with the knowledge of your impending investigation. It is very useful to have accounts close up to the date of your investigation, but it can have its disadvantages.

Whilst dealing with the liabilities of the business; do not forget the taxation position. This is particularly important in these days where an available carry forward of losses may be of considerable importance to a position. Also, you should find out whether the liability is agreed and is included in the accounts, or if there is any outstanding difficulty with the Inland Revenue Authorities.

The products of some businesses have a contingent liability attached to them under guarantee or otherwise. In such cases you must consider this liability and what provision has been made for it. Also, what has been the experience in the past in this direction.

You must now turn your attention to the question of the contractual commitments and liabilities of the business as regards purchases. Also, it will usually be found necessary and convenient at this stage to consider the extent and value of the orders on the books. In considering the order book, needless to say you must have some regard to whether the orders will ever be taken up and the standing of the customers. You should be able to ascertain whether the orders can be completed from stock and by taking up the purchase contracts, or whether further buying will be required; in other words, whether the business is overbought or oversold. In some industries—for example, our wool textile industry—this question is of almost paramount importance in assessing the position of a business, the reason lying in the violent fluctuations occurring in the market price of the necessary raw material. There are other industries where the question is of equal importance. Further, note it is not sufficient to know the extent to which the business is overbought or oversold; you must know what potential profit or loss is concealed in such a position.

In the wool textile and similar industries you must ascertain what has been the buying policy of the management if you are to understand fully the reasons for the results disclosed by the accounts. For instance, during the past three years most businesses where the policy has been to overbuy consistently might be expected to show losses apart altogether from any other consideration. If you reach the conclusion that the policy of the management has resulted in losses you may have to try to assess the damage to see how the business has functioned apart from such losses.

I regard this as an entrancing side of the work on many investigations, but I must pass on to costing, and what you may learn from that source.

I have already referred to the fact that any existing cost records may be worth examination. If you are making an investigation to find out what is happening to a business this side of the work is of particular importance, as you must endeavour to ascertain whether there is any fundamental error affecting the selling price obtained or the judgment of the management. During recent years we have almost got used to the idea that you have to sell an article for what you can get for it and according to the degree of "sales resistance" experienced from competitors. In such circumstances, costings seem of little value, but, in actual fact, accurate costings have their use even in such times as providing a useful guide on which to obtain business, since it is a poor way of doing business to be always following your competitors' quotations. The business you are investigating may be suffering in that way or by attempting to obtain prices which are not competitive, based upon inaccurate or badly designed costings.

At some stage in the work, if the business under inquiry

be a limited company, you will have called for the statutory books and the minute book. Sometimes there are records of meetings of the management which provide useful reading. Sometimes, too, you will find it desirable to call for and peruse the various agreements in which every business seems to entangle itself.

You will now be reaching the point when you will have gathered the necessary information, formed your opinions, and can commence to write your report. Now let me say at once that this is not the easiest part of the work. I am one of those who believe that your report should not be limited to a statement of facts, but should lead to definite conclusions and give definite advice. If you are advising a client who is considering an investment you must, of course, give him tabulated results and indicate what you consider to be the future possibilities of the business, and why. Amongst other things you must tell him are whether the business is declining or improving, and why; what you think of the management; what your examination of the assets and liabilities has disclosed; the measure of his risk with advice as to the best form for his investment. Naturally, unless you are certain that the business is sound, efficiently managed, and has possibilities of absorbing and profitably using new capital, you will say "no" to your client.

If, on the other hand, you are advising someone who is already involved in the business—for instance a shareholder, or more probably a creditor—your outlook and report must be rather different. First of all you have to decide whether the business can succeed or not; that is to say, whether it can succeed if your recommendations are carried into effect. If you yourself are satisfied that it cannot succeed in any event, it is your duty to say so, and in no uncertain manner, of course giving reasons. If this be your view, you will show that the business is declining and must continue to decline despite any economies which can be made or other steps which may be possible. If you can prove this or indicate its likelihood by figures in your report, you must, of course, do so. Let us hope, however, that as a result of your examination you feel certain of a happier outcome. Now you have to suggest remedies, and again you must prove your case both to your own satisfaction and that of your client. If you have decided on economies you must indicate what they are and the total amount of annual saving which can be effected. If you think some improvement in selling activity is needed, you must indicate the directions. If you are of opinion that departments should be closed or opened, or whatever steps are desirable, you must give the fullest advice in your power. Briefly, your models must be working models, and you must not advise the carrying on of the business or the sinking of fresh capital in a venture unless you are reasonably certain that on the adoption of your recommendations the business can be saved.

Your Honorary Secretary has given me a very big subject, and in the time at my disposal I have only been able to give you a very general outline of the work which you may find necessary on an investigation. I am well aware that there are many things I have not mentioned. My aim, however, has been to interest the students present in this very important branch of our work and to provide food for thought rather than the fullest of meals. Some of you may be disappointed because I have not given you any personal experiences. To those I would say that I am not yet old enough and, perhaps, not so unwise as to indulge in reminiscences.

No two investigations are quite alike, but most cases will respond to treatment on lines similar to those I have indicated, and if, in addition, you have used your eyes and ears and your common sense, I am sure on finishing your report you will feel satisfied with it. What is more, time will prove the wisdom and good sense of your advice, than which there cannot come to you greater cause for satisfaction.

Reviews.

Cost Accounts. *By Walter W. Bigg, F.C.A., F.S.A.A. London: Macdonald & Evans, 8, John Street, Bedford Row, W.C.1. (294 pp. Price 10s. 6d. net.)*

This is a useful book on the subject of costing, dealing as it does with all sections in considerable detail including contract costs, process costs, single costs and standard costs, and embodying a chapter on the reconciliation of the cost and financial accounts. Numerous forms with specimen entries are given in illustration of the text, and each chapter is followed by a number of questions selected from the examination papers of the Society of Incorporated Accountants and Auditors and other accountancy bodies. The author shows an intimate knowledge of his subject.

Complete Practical Income Tax. *Sixth Edition. By A. G. McBain, C.A. London: Gee & Co. (Publishers) Limited, 8, Kirby Street, E.C.1. (296 pp. Price 7s. 6d. net.)*

The arrangement of this publication is very convenient, and the matters discussed are mainly those where difficulties are likely to arise, as for instance allowances and reliefs, residence, Dominion Income Tax, Depreciation, Repairs and Renewals, Loss Claims, New and Discontinued Businesses. Numerous examples are given showing the working out of claims and the preparation of returns.

The Law of Arbitrations and Awards. *By Horace S. Palmer, M.A., Barrister-at-Law. London: Sir Isaac Pitman & Sons, Limited, Parker Street, Kingsway, W.C.2. (160 pp. Price 6s. net.)*

The primary object of the author is to cover the subject in sufficient detail to meet the requirements of students for the examinations of accountancy bodies and certain other institutions. Hence only the main principles are dealt with. The book, nevertheless, contains a large amount of information which will be found useful to anyone who may be acting in the capacity of Arbitrator. The matter is well arranged and clearly stated.

Petroleum Distribution Accounts. *By Joseph Johnson, A.C.I.S. London: Gee & Co. (Publishers) Limited, 8, Kirby Street, E.C.1. (126 pp. Price 8s. net.)*

The system described by Mr. Johnson is one which has been in actual operation in a leading Petroleum company and has been found to give satisfactory results. We believe, also, the book is almost the only one on the subject which has been published. After describing the method by which the distribution of Petroleum is carried out, Mr. Johnson explains the chief documents used in recording the transactions, and then proceeds to deal with the book-keeping, including hire-purchase transactions, statistical returns and internal checks on error or fraud. Invoicing and posting by machinery is also explained. In a final chapter a description is given of the "slip" system which is a system designed to effect economies in clerical costs by using only the barest minimum of records. The appendix contains numerous forms and some illustrations of modern appliances used in the account keeping.

Status and Duties of Secretaries and Directors. *Tenth Edition. By Herbert W. Jordan and Stanley Borrie. London: Jordan & Sons, Limited, Chancery Lane, W.C.2.* (138 *pp. Price* 3*s.* 6*d. net.*)

Secretaries and Directors will find in this little book very concise information and advice on points of difficulty that arise in carrying out their duties. Part I relates to secretarial work and Part II to Directors, whilst Part III deals with the obligations of both secretaries and directors in relation to allotments, minutes, meetings, transfer of shares, extraordinary and special resolutions, increase of capital, &c.

Banking Credit and the Crisis. *By J. W. Kempster, D.L., M.I.E.E. London: London General Press, 6, Bouverie Street, E.C.4.* 386 *pp. Price* 12*s.* 6*d. net.*)

This is a somewhat formidable book dealing with a very difficult subject and containing many facts and statistics as well as expressions of opinion. In a foreword Sir Josiah Stamp says that without in any way pretending to identify himself with the whole of the facts and opinions appearing in the book, it is clear that the author attacks the problem in an exceedingly commendable and useful way because the factual basis is extensive and well considered. He also adds that no work of such a wealth of reasoned detail has appeared since England went off the Gold Standard. Coming from so eminent an authority this must be regarded as a high recommendation. The book is divided into several parts, the first dealing with banking, the second with credit and co-related problems, and the third with the crisis and the causes of depression peculiar to Great Britain. The fourth part discusses tariffs and the final part gives the author's conclusions, including his views as to the future of this country. The work contains much that is interesting and displays a wide knowledge of the subject.

A Simplified Guide to Rating and Assessment. *By Dennis R. Cockshaw. London: Gee & Co. (Publishers) Limited, 8, Kirby Street, E.C.1.* (62 *pp. Price* 3*s.* 6*d. net.*)

This little book deals with the principles of assessment in areas outside London. As an official of a rating authority the author is well qualified to write on the subject. Amongst the matters discussed are: how assessments are ascertained; the recovery of rates; the valuation lists, their effect, and how they can be amended; also as to the ratepayer's remedies by way of appeal and otherwise. Full information is afforded as to how and when objection should be made, and generally as to the procedure to be adopted.

Law for Laymen. *By H. D. Greeley. New York: American Institute Publishing Company Inc.* (348 *pp. Price* $3.50.)

The object of the author in writing this book is to present a short statement of American law in relation to the subjects which mainly concern commercial transactions. It is accordingly of special interest to accountants and business men. Mr. Greeley has endeavoured to convey an understanding of the legal principles and an acquaintance with the procedure by which those principles are applied. The book covers a wide range of law, and it must have entailed a prodigious amount of work to collect and set forth even the fundamental principles. Some idea of the wide scope of the work will be gathered from the fact that it includes the law relating to contracts, agency, real property, mortgages, personal property, company law and partnership, landlord and tenant, patents and trade marks, negotiable instruments, insolvency and bankruptcy; also a chapter on wills and trusts. The book is a valuable one for anyone in this country to possess who is concerned with business transactions in America.

THE POST OFFICE ENQUIRY.

The following are extracts from the Report of the Committee appointed by Parliament to enquire and report as to whether any changes in the constitution, status or system of organisation of the Post Office would be in the public interest. The Committee consisted of Viscount Bridgeman, LL.D. (chairman), Lord Plender, G.B.E., and Sir John Cadman, G.C.M.G.

RELATIONSHIP TO THE TREASURY.

10. From the financial aspect the position of the Post Office as a revenue-producing Department is emphasised by the fact that revenue and expenditure are kept entirely separate, the former being paid over intact to the Exchequer and the latter being voted by Parliament on the annual Estimates, with the exception of capital expenditure on telephone and telegraph construction and on Post Office sites and buildings. Such capital expenditure is financed by loans, representing the estimated expenditure for a period of years, raised by the Treasury from the National Debt Commissioners and repaid through annuities which are charged upon the Post Office vote. The loans outstanding as at March 31st, 1932, amount to some £95,000,000, and the provision for annuity payments (covering interest and amortisation) in the estimates of the current year amounts to some £9,645,000.

11. Inasmuch as the Post Office Estimates and Appropriation Account on the one hand, and the entries relating to Post Office business in the National Finance Accounts on the other, are merely statements of cash expenditure and cash receipts by the Post Office itself, they give no true picture of the financial results of Post Office operations for the year. No payment is made to the Post Office for services rendered to other Government Departments, such as the transmission of official correspondence, the management of National Savings Certificates, and the payment of Old Age and War Pensions. Conversely, the Post Office is not debited with the cost of certain services rendered to it by other Government Departments, *e.g.*, the maintenance of buildings and the provision of furniture by the Office of Works, and the provision of stationery and printing by the Stationery Office.

SUGGESTED MODIFICATIONS IN THE FINANCIAL STATUS OF THE POST OFFICE.

62. The existing financial relation of the Post Office with the Exchequer has, in general terms, been described in paragraphs 10-11. It rests, as is required by the National financial system, on a strictly cash account basis. The Post Office pays over weekly to the Exchequer its gross revenue receipts which thereupon become part of the National revenue; it draws weekly from the Exchequer the amount required to meet its current cash disbursements so far as these are provided for in the Post Office Vote. The surplus of receipts by the Exchequer over issues from the Exchequer appears in the Budget and in the National Finance Accounts as the "Post Office Net Receipt."

63. The balance of these cash transactions does not, taken by itself, represent the profit in a commercial sense earned by the Post Office. For instance, in determining the commercial profit or loss it is necessary to take account of the accruing actuarial liability for pensions of the existing personnel, whereas what enters into the cash transactions is the pensions now paid to the personnel of an earlier period. Thus it has happened that, until recently, the pension liability accruing annually has been

a greater sum than the annual pension payments, while at the moment the current pension payments exceed the actuarial liability; in effect the Post Office is drawing for its current pensions on the theoretical accumulation of previous years. Similarly the cash transactions do not show revenue earned but not actually received within the year, or liabilities incurred but not actually discharged within the year, nor do they include depreciation or obsolescence; whilst, on the other hand, the cash payments do include the amortisation of Loans. Again, an important part of the requirements of the Post Office in respect of buildings, furniture, stationery, rates on premises, &c., is paid for not out of the Post Office Vote but out of the Votes for Works, Stationery and Rate contributions; while, on the other side of the account, the Post Office Vote includes expenditure of various kinds on behalf of other departments for which it does not receive repayment.

64. In our view modification of these arrangements in material particulars is desirable, if the Post Office is to be regarded, and managed, as a self-supporting organisation.

We are of opinion that in place of the present "Post Office Net Receipt" the Exchequer should receive a definite contribution (the amount and character of which we discuss in the following paragraph), and that the residue should be made available for the improvement and development of Post Office facilities and services to the public.

65. In determining the basis of assessment, and amount, of that contribution we have first to deal with certain classes of revenue and expenditure already mentioned. These are :—

(*a*) Work done for the Post Office by other Government Departments but not paid for.

(*b*) Unpaid services rendered by the Post Office to other Government Departments.

(*c*) The net receipts from Wireless Receiving Licences after meeting the cost of collection and management and the proportion payable to the British Broadcasting Corporation.

(*d*) The excess (or short fall) of actual pension payments over the accruing actuarial liability for pensions of the existing personnel.

66. We are of opinion as regards these four items—

(*a*) *That for reasons of administrative and business efficiency the Post Office should pay for services rendered to it by other departments, such as the provision and maintenance of buildings, the supply of printing and stationery, and rates on Post Office buildings.*

(b) *That, similarly, for services rendered by the Post Office to other departments payment should be made.*

(*c*) *That the Exchequer, and not the Post Office, should be entitled as at present to the net receipts from Wireless Receiving Licences.*

(d) *That the burden of cash pension payments in excess of the actuarial liability in respect of current personnel should fall on the Exchequer, and not on the Post Office customer, seeing that the Exchequer (in other words the taxpayer) must be presumed to have received in past years an appropriate actuarial contribution for the cash liabilities which now fall to be met.*

67. The effect on the accounts if these adjustments were made would be as follows: we use the latest figures given to us by the Comptroller and Accountant-General of the Post Office for the year 1932-33 which must only be taken as estimates :—

(1) Revenue collected by Post Office		£70,400,000
Less (2) Post Office Vote payments (on present basis)		59,188,000
"Post Office Net Receipt" ..		11,212,000
Add (3) for work done by Post Office for other Departments		2,785,000
		13,997,000
Less (4) for work done for Post Office by other Departments ..	£1,595,000	
(5) Net receipts from Wireless Licences	884,000	
		2,479,000
		11,518,000
Add (6) Excess of pension payments over pension liability ..		778,000
Net surplus ..		£12,296,000

68. In the present state of the National finances it would be impracticable to suggest any other principle than that the Exchequer should retain out of the net revenue collected by the Post Office a sum approximating to the amount which it is at present receiving, subject only to any variation in the amount of items 3, 5 and 6 in para. 67 above, which for the reasons stated ought, in our view, to affect the Exchequer and not the Post Office customer: on the other hand the Exchequer net receipt ought not to be diminished or increased by any variation in the expenditure on work done by other Departments for the Post Office. In the last three years the figures corresponding to the £12,296,000 above-mentioned have been £10,654,000 in 1929-30, £10,754,000 in 1930-31, and £12,303,000 in 1931-32. The large increase in the last-named year is more than accounted for by the drop in the cost of living bonus.

On these figures and on the basis of the foregoing adjustments, a fixed contribution of £11,500,000 *plus* 50 *per cent. of any excess over that figure, would, in our opinion, be an appropriate sum. Any marked alteration in the present level of wages or in the postage rates of inland letters would obviously necessitate reconsideration of the contribution.*

69. In recommending that the Exchequer should share to the extent of 50 per cent. in any excess over £11,500,000, we have had in mind the fact that the growth in the pension payments over pension liability (which we understand may go on for some time) will operate adversely to the Exchequer, and whilst in principle we think this burden should fall on the Exchequer (see para. 66 (*d*), we feel that it may be inexpedient, for the time being, in view of the state of the National finance, to put this charge on the Exchequer unless they receive as a set off a share in the growth of the net receipts for a limited period.

If it should be decided that the principle of inter-departmental payment for services rendered or other liabilities incurred shall not be applied to the extent which we recommend, then, in order to arrive at the cash contribution payable to the Exchequer out of the net receipts actually held by the Post Office, the basic contribution of £11,500,000 would be subject to adjustment each year in respect of the special items 3 and 4 mentioned above in para. 67 as well as in respect of items 5 and 6.

We suggest that the amount of the contributions should be reviewed after three years.

70. The annual accounts prepared on a commercial basis are designed to show the commercial profit or loss as between the Post Office and its customers and therefore show somewhat different results. The commercial method seems to us to be a more correct principle for an arrangement with the Treasury than a cash basis, but in the absence of a separate fund for the business of the Post Office, outside the Exchequer, the principle is difficult to apply. We think, however, that this matter should be further considered when the review of the amount of the contribution takes place after three years experience.

71. A contribution of this kind is intended to cover various matters in regard to which it seems to us proper that the Post Office customer should make payments, such as interest on capital expenditure provided by the Exchequer in past years in excess of outstanding loans, Income Tax under Schedule A, the services of the National Debt Commissioners with regard to the provision of capital, and consideration in the nature of a royalty for the monopoly conferred by Parliament on the Post Office in regard to its principal classes of business.

72. The annual surplus after settlement with the Exchequer should be carried to a separate fund outside the Exchequer and made available for the purposes already indicated. The approval of the Government of the day, or at any rate of the Chancellor of the Exchequer, should be required as to the specific application of the fund from time to time. Pending its application it could be invested temporarily with the National Debt Commissioners, *but we wish to make it plain that in our view it should be a Post Office fund and not a Treasury fund.*

73. As regards the provision of capital required for Post Office development, principally in connection with the Telephone system, we are of opinion that it is neither necessary nor desirable that the Postmaster-General should possess an unrestricted power of borrowing, whether in the market or otherwise. Indeed, no material modification of the present arrangements, under which the Post Office borrows from the National Debt Commissioners within limits sanctioned by Parliament and the Treasury, appears to us to be necessary, so long as the Treasury are prepared to meet, as they have done in the past, the legitimate and reasonable demands of the Post Office in this respect. If as a result of increased demand, stimulated by a more active commercial policy, the future capital requirements of the Telephone Service are substantially increased, we feel sure that the Treasury will, as they undoubtedly should, facilitate the provision of the necessary funds through the National Debt Commissioners.

THE DEFECTS OF THE EXISTING ORGANISATION.

96. The Post Office Secretariat has come to assume a position which has no parallel in the Secretariat of any other Government Department and is in fact the sole source of authority under the Postmaster-General. For instance, we understand that no executive department of the Post Office can give an instruction to another department, nor can it through its own officers do anything for which it has not Secretariat authority, either general or specific. By virtue of its autocratic position the Secretariat has come to acquire a status out of proportion to that of other Post Office departments.

97. Moreover, the present position of the Secretariat contravenes what has come to be recognised as one of the fundamental principles of organisation, viz: The distinction between policy and practice, between the administrative and the executive functions. The neglect of this important distinction we regard as one of the main weaknesses of the existing Post Office organisation. It may not be inappropriate to quote the words used by the Esher Committee nearly 30 years ago on this point, in regard to the organisation of the Army:—"Attempts to combine the administrative and executive functions of the Army have led to confusion, to reduplication of work, to expense, to dual control, to divided responsibility . . ." The Secretariat of the Post Office, as at present constituted, is concerned not only with the framing and formulation of policy and with the supervision of its execution, but also with the conduct of the daily business of the Post Office services, for which it is unsuited, both by training and experience.

98. We have formed the impression that individual members of the Secretariat possess considerable administrative ability but that the usurpation of executive functions by the Secretariat, as a body, has in some cases deflected this ability into channels for which it is less well suited.

99. The administrative staff of the Secretariat are recruited through the ordinary Civil Service Administrative Class Examination; on joining they are appointed to the Secretariat, and although in the first years of their service they may be detached for a few months to the provinces for service under a Surveyor, they have had quite inadequate opportunity to acquire any thorough training in or experience of, the actual executive work of the Post Office. Handicapped as they are by this absence of experience, they spend the remainder of their official career, not merely in administering, but to a considerable extent in controlling, the execution of services of which they may have considerable theoretical, but little practical, knowledge.

This absence of touch with the work "in the field," and consequent immunity from personal contact with the public, has perhaps tended to breed in some cases a certain aloofness and apparent indifference to the demands of the public which is probably at the root of the criticism that the Post Office attitude is one of "take it or leave it."

100. The autocratic isolation of the Secretariat in relation to the Engineering and Accountant-General's departments and the narrow and specialised meaning attached to the word "Administrative" in respect to staff generally, in our opinion, prevent these two departments from taking an adequate part in the general scheme of control.

101. In his own domain there is no evidence that the engineer is unduly hampered or that this department is inefficient or unprogressive—indeed the evidence is to the contrary. So much so indeed, that we would take this opportunity of recording the high opinion we have formed of the capacity in general of the engineering and technical staff, and equally of the department of the Controller of Stores. But we believe that engineering experience is insufficiently brought into the consideration and formulation of general policy.

We think that this incomplete synthesis of the administrative and the technical sides tends to result not only in the administrative side failing to give due weight to technical considerations, but also in the technical side failing to realise adequately the importance of administrative principles.

102. Similarly we believe that the separation of the Accountant-General's department, with the general efficiency of which we are much impressed, has resulted in financial control being to a large extent confined to the exercise of *ex-post facto* criticism, instead of manifesting itself by active participation in the administration.

103. The centralisation of administration and the higher executive functions in the Secretariat has tended to denude the Surveyor and the provincial staffs of real responsibility and authority, and has inevitably imposed an undue rigidity where, in contact with the public, flexibility is required.

104. Finally, the divorce of the engineering and administrative sides, to which we have already referred, has tended to produce duality of control and absence of co-ordination, while the separation of finance, and the instruments of finance, from administration has militated against real decentralisation because machinery for measuring performance, which effective decentralisation requires, does not exist.

105. As regards the general structure of the provincial organisation, the system would appear to us in regard to Postal services to be well devised to meet requirements. Head Postmasters and Sub-office Postmasters should be allowed a somewhat freer hand, particularly in regard to staff, but we believe that these and similar improvements will come automatically, if and when the major changes in organisation which we recommend become operative. In our view the main weakness of the system of provincial organisation is that which permeates the Post Office as a whole, viz: The separation of the technical and the directive side into watertight compartments, with consequent absence of proper correlation at the appropriate stage. This weakness manifests itself particularly in the Telephone Service.

GENERAL CONCLUSIONS.

127. *To sum up:—We do not consider that the change in the status of the Post Office to that of a Public Utility Company or Statutory Authority, either wholly or in part, is desirable. In the public interest we feel that the Parliamentary control which exists at present is essential in a business of such a national character. Nor do we feel assured that a change of this kind would remedy the alleged defects of administration.*

The criticisms, so far as we find them to be justified, in our opinion point to defects in the present organisation which can be remedied without such a complete change of status.

128. The first of these defects is over-centralisation at Headquarters. In the Post Office the Secretariat has acquired a dominating power which has imposed on the service a bureaucracy more rigid than that of any other department.

We suggest that instead of the present system, a Board should be established representative of the various functions involved; that the Chairman should be the Postmaster-General and that a Director-General who would in effect be a General Manager, should act as Deputy Chairman, and that the policy of the Post Office should be decided by the Board, and carried out all over the country by a reorganisation of staff, of which details are given in paragraphs 113-125, *and in accordance with the principles indicated in paragraph* 108. *This would give more freedom of action in matters of detail and more authority to provincial officials.*

129. The other most serious defect we think is the fact that all the Post Office profits are taken by the Treasury. This removes from the Post Office a natural incentive to progress and economy. *We realise that a large sum is required by the Chancellor for Revenue, but we think that this sum might be fixed for three years at some figure approximate to the present amount which the Revenue absorbs, and that any savings above that amount should be available for improvements in the service, subject to the least possible interference by the Treasury. Details will be found in paragraphs* 62-73.

130. The effect of our two principal suggestions should be to give greater freedom and elasticity to the service, and more opportunity to the experts to utilise their skill and experience in the advancement of the efficiency of the service, and in the interests of the public.

131. *In an organisation such as the Post Office, which depends so much upon scientific discoveries and developments and their practical application, we consider it essential to bring engineering and research into more intimate touch with the general problems of administration. The object of this closer relationship is two-fold; the engineer, on the one hand, will be in a position to visualise the picture as a whole, and thus to direct his activities into those channels where the need for progress and development is greatest; while, on the other hand, those who are charged with the day-to-day running of the administrative machine will be able to avail themselves of the scientific point of view to the fullest extent.*

132. Our other main recommendations, details of which will be found in our Report, may be briefly summarised as follows:—

(1) *The Telegraph Service should be completely amalgamated with the Telephone Service* (*para.* 24).

(2) *Attention should be paid to the systematic training for the supervision of personnel employed upon telephone construction and maintenance* (*para.* 27).

(3) *Consideration should be given to the standard of telephone construction in thinly populated areas* (*para.* 28).

(4) *The objections to the employment of women telephone operators up to* 11 *p.m. should be reconsidered* (*para.* 32).

(5) *Staff management should be decentralised to the fullest possible extent and the right of appeal to Headquarters should be restricted* (*para.* 40).

(6) *The existing relationship between the Post Office and the Office of Works in regard to the provision and maintenance of accommodation, furniture, etc., should continue* (*paras.* 75-77).

(7) *Stationery Office.*

(a) *The ordinary departmental printing common to Government Departments should continue to be done by the Stationery Office.*

(b) *Directory printing should remain with the Stationery Office but the Post Office should have access to Stationery Office accounts and should be entitled to refer charges under dispute to the Treasury.*

(c) *Security, including stamp printing, required for Post Office Services should be put out to competitive tender, the Stationery Office being invited to tender together with outside firms.*

(*paras.* 81-82).

(8) *The Advisory Council should be consulted by the Postmaster-General on questions of general policy and be regarded as a connecting link between the Post Office and the public* (*para.* 126).

133. Before concluding our report we wish to take the opportunity of making some general observations, which, we think, merit attention.

Recognising that there are certain defects in the Post Office system of organisation, we have attempted to suggest how these defects can, in our opinion, best be remedied. At the same time we wish to place on record our opinion that on the whole the Post Office performs the services for which it is responsible with remarkable efficiency. If we have criticised the organisation and

drawn attention to certain shortcomings, we have done so in the hope that such criticism will prove constructive.

134. While it may be true that the attitude of the Post Office towards its clients, the public, does on occasion show a certain lack of imagination and adaptability, it is perhaps equally true to say that the attitude of the public towards the Post Office leaves something to be desired. No organisation can fail to be adversely affected when on the one hand it is denied credit that is its due, and on the other is subjected to continuous and often unfair and uninformed criticism. In such circumstances the staff cannot fail to become disheartened and demoralised. From the evidence we have heard and from personal observation we believe that the vague generalisations as to inefficiency and discourtesy on the part of the subordinate staff are exaggerated. Instances do undoubtedly occur, but we believe that the staff as a whole are genuinely anxious to give their best service to the public, and we see no reason to believe that they compare unfavourably so far as efficiency is concerned with any other body of employees of similar magnitude.

135. As regards the higher directing and controlling staff both administrative and technical, we have formed the impression that it comprises men of first-rate ability judged by any standard. It is, however, vital that the existing system should be so modified as to enable a better use to be made of such material, and a fuller scope given to the capacity and initiative that we are confident exists; it is our belief that the adoption of our recommendations will have this effect.

136. The Committee have received every assistance from the Post Office in the course of their enquiry and have been impressed by the ability, candour and freedom from prejudice of all the official witnesses who have given evidence before them.

137. We wish to put on record our very warm appreciation of the able services rendered by Mr. Austin Earl, C.B.E., our secretary. He has been indefatigable in ascertaining all the information for which we asked, and in arranging the business of the Committee with skill and consideration for ourselves and all the witnesses and others who have been concerned. We are greatly indebted to him for the invaluable help he has rendered to our Committee.

District Societies of Incorporated Accountants.

LONDON.

Programme, 1932-33.

1932.

Oct. 12th. Luncheon. Principal guest, Mr. E. Cassleton Elliott, F.S.A.A., President of the Society of Incorporated Accountants and Auditors.

Nov. 18th. Reception and Dance at Incorporated Accountants' Hall.

Dec. 6th. Lecture by Professor T. E. Gregory, D.Sc., at Incorporated Accountants' Hall.

1933.

Jan. 24th. Lecture by Mr. Robert Ashworth, F.S.A.A., on "Some Aspects of Group Finance," at Incorporated Accountants' Hall.

Feb. 22nd. Luncheon. Principal guest, Dr. Cyril Norwood, M.A., Headmaster of Harrow School.

Mar. 31st. Reception and Dance at Incorporated Accountants' Hall.

April 25th. Lecture by Lord Melchett on "Accountancy Methods as a factor in the Economic System," at Incorporated Accountants' Hall.

BOMBAY.

ANNUAL MEETING.

The annual general meeting was held on June 25th, when the report for the year was submitted and adopted

ELECTION OF OFFICERS.

The following office-bearers were elected for the ensuing year:—President, Mr. Sorab S. Engineer; Vice-President, Mr. F. R. Merchant; Committee, Mr. N. M. Raiji, Mr. M. R. Tambe, Mr. R. K. Dalal, Mr. B. M. Mody, Mr. K. N. Pagdivala, and Mr. M. P. Mistry; Hon. Auditor, Mr. J. H. Patel; Joint Hon. Secretaries, Mr. A. K. S. Aiyar and Mr. E. J. Dastur.

Report.

The Hon. Secretaries have pleasure in presenting to the members the third annual report of the District Society.

ACCOUNTS.

The accounts have been made up for the fifteen months ending March 31st, 1932, as the closing date had to be changed from December to March under the new rule sanctioned by the Parent Society.

MEMBERSHIP.

The members on the roll on March 31st, 1932, numbered 30, of which four were resident outside Bombay.

GENERAL.

The second Anniversary Souvenir was published during the period, containing an account of the second annual dinner, at which a large and representative gathering was present.

Two papers were presented to the members: One on "Income Tax Assessment and Procedure," by Mr. F. R. Merchant, F.S.A.A., Assistant Commissioner of Income Tax, Bombay, and another by Mr. M. P. Mistry, Incorporated Accountant, on "Some Practical Aspects of Income Tax Law."

Representations were made to the Parent Society in regard to changes in the Rules of that Society specially affecting candidates from India, but the Council did not see their way to make any material alteration.

A memorandum was sent to the Government of India regarding the new All-India Accountancy Board, and some of the suggestions made by our Society have been incorporated in the new Auditors' Certificate Rules, 1932.

EAST ANGLIA.

Annual Report.

The Committee have pleasure in presenting their Report for the year ended March 31st, 1932.

They desire to place on record a very cordial expression of thanks to those gentlemen who gratuitously gave lectures during the session.

MEMBERSHIP.

The area governed by the District Society comprises the counties of Norfolk and Suffolk and the Isle of Ely. The present membership is 109, including 21 Fellows, 53 Associates, and 35 students.

LECTURES AND MEETINGS.

The following lectures and meetings were held during the 1931-32 session, the average attendance being 27 :—

"New Taxation of Land Values," by Mr. T. F. Southall, Barrister-at-Law.

"Trusteeships," by Mr. F. T. Alpe, Barrister-at-Law.

"Duties and Liabilities of Auditors," by Mr. W. H. Grainger, F.S.A.A.

"Conversion of a Business into a Private Company," by Mr. H. W. Jordan.

"Income Tax: Some Knotty Points," by Mr. T. G. McKenna, H.M. Inspector of Taxes.

"Banking," by Mr. A. A. Emmett.

Ten-Minute Papers by Members.

"Negotiable Instruments," by Mr. C. A. Sales, LL.B., F.S.A.A.

"Notes on Auditing," by Mr. W. P. Gill, A.S.A.A.

The Committee extended the number of lectures held during the year, as compared with the previous year. They would like to see a larger attendance, particularly of the student members, since the lectures are designed to assist them in their studies, and the lecturers are all authorities on the particular subjects dealt with by them. The thanks of the Committee are due to the members who volunteered to give ten-minute papers.

The first annual dinner of the Society was held on July 24th.

EXAMINATIONS.

Six members of the Student Section passed the Final examination of the Parent Society, and the Committee desire to congratulate them on their success.

DISTRICT SOCIETIES' CONFERENCE.

The Secretary attended the Conference of the representatives of District Societies held in London in May, 1931, at which matters pertaining to the regulations of District Societies and other matters of professional interest were discussed.

LIBRARY.

The Committee have decided to set up a Library at the earliest possible moment, and steps are being taken to house it. A committee comprising Mr. R. G. Acock, Mr. F. G. Platten, the Secretary and a student member has been appointed to deal with the matter.

SOUTH WALES AND MONMOUTHSHIRE.

(CARDIFF AND DISTRICT STUDENTS' SECTION.)

An enjoyable cricket match took place on August 4th between teams representing the Cardiff Incorporated Accountants' Students' Society and the Cardiff Chartered Accountants' Students' Society. The Incorporated Students batted first on a fine wicket, and as a result of useful scores by B. Horspool and R. R. Davies compiled a total of 85. The Chartered Students, however, thanks to a fine stand by C. C. Hill and D. M. Horspool, scored 92, and thus won by seven runs. This was the first cricket match arranged between the two Societies; it is hoped that the event will become an annual one.

The directors of the Midland Bank Limited have paid an interim dividend for the half-year ended June 30th last at the rate of 16 per cent. per annum, less income tax.

Conversion of a Business into a Limited Company.

A PAPER read before the Incorporated Accountants' Society of Manchester and District by

Mr. HALVOR PIGGOTT,
INCORPORATED ACCOUNTANT.

Mr. PIGGOTT said: The subject of my paper is one which, sooner or later, in all probability, has to come under the consideration of every practising accountant. It is not a new subject, as it has occurred from the early days of limited companies, it occurs now, and is likely to go on so long as limited companies continue to be formed, but though it is continuously happening, a conversion is not an everyday occurrence in an accountant's office. Although, no doubt, most of you will have had some experience of this subject, an interchange of ideas is always useful.

The desire for conversion of a business into a limited company may arise from various reasons. I doubt whether I could give a really comprehensive list of whys and wherefores, but in mentioning just a few that occur to me the following will suffice to show how varied the reasons can be.

There may be the need for new capital to be introduced either to enable the business to carry on, or possibly to extend the business. Conversion might be desirable to facilitate amalgamation or merger with another firm. Possibly there is need to replace a deceased or retiring partner's capital. A conversion scheme might make more convenient or economical the disposal of a person's interest in the business. A proprietor might wish to give or sell an interest in his business to relatives or employees without relinquishing control. Possibly the purpose of safeguarding the personal estates of a proprietor or partners is needed.

Sometimes there is more than one reason for the proposed conversion, but whatever the reasons, any scheme of conversion must be prepared from the point of view of giving effect to, and fitting in, with the reasons. This point is of the utmost importance. If one should be consulted on the subject, this point is the one that must receive primary consideration. The reason that may be offered initially may be only one of several, and that perhaps not necessarily the most important. It is in such case that the exercise of qualities of tact and discretion will be called fully into play, and the fact that you may have previously built up a strong feeling of confidence, and possibly friendship, will be of the utmost value. Clients do not always state at once exactly what is in their mind, and your object, if you are to be called upon to prepare any scheme, is to get at the real reasons, and know your client's mind on the matter, as only then will the scheme prove to really meet his needs. You must invite the fullest confidence. Your past knowledge of the business and the client and/or his partners, employees, relatives, &c., must all be reviewed in the light of his first stated reasons. A judicious inquiry or suggestion thrown into the conversation here and there will probably provide a new facet from which you will get a gleam of light, and you will therefore gradually build up a full understanding of the real requirements of the case, which may confirm the original reason or amplify it by reasons which are of equal, if not greater, importance. The fact that I wish to emphasise is that, like every other matter which comes before an accountant for consideration, reasons must be tested, and not necessarily accepted at

their face value. Once one is satisfied as to the real requirements, then one can give definite consideration to the best methods to be employed and design a scheme which should secure the desired results.

It may be that the proposed conversion does not originate from your client, but from yourself. There are times when one may with advantage point out to clients the value of converting their businesses into limited companies. Not every business is suitable, nor is it invariably desirable even if suitable. The accountant, therefore, if he is to suggest such a course, must himself be prepared with real and tangible reasons for his suggestion. In such circumstances the advantages and disadvantages of the proposal must be clearly placed before the client in order that he may judge whether the proposition is one which should go forward or not.

Let us assume that it is decided to proceed. The first matter that will be decided upon is whether the conversion is to take the form of a private limited company or a public limited company. As I have already stated, the scheme must be prepared from the point of view of the objects to be attained. As these objects can vary so very greatly, any attempt to set down general lines would not be very helpful—each case must be treated upon its own merits, it must receive the fullest consideration, and a scheme drawn up accordingly. I can, however, take a few examples which might be considered as typical, and roughly indicate the lines upon which a solution has been worked out. A great many of the steps leading to the final result are, of course, more or less common to all schemes, and they will no doubt be readily recognised by you.

FIRST EXAMPLE.

My first example is that of a moderate sized manufacturing concern. Originally there were three partners: the nature of the business was very steady, and though the profits were not large, they had been sufficient to provide a steady income for each partner. With the passage of time, first one and then another partner died, and on each occasion the deceased partner's share had been bought by the survivors. At the time of conversion there was only one proprietor, who was getting on in years. He had a wife, three sons and two daughters. The business was his main asset, and though he was desirous that his three sons should succeed thereto he also had to consider making proper provision for his widow and his two daughters. In addition, he was anxious to ease off somewhat without actually handing over control of the business entirely. His wishes expressed themselves in the form that his widow should have a life interest in his estate to such extent as would produce a certain minimum figure. He was also desirous of settling the division of his business between his sons and daughters in such a way as would obviate any possible dispute arising on his death, and so that they would also be able to have an immediate interest and benefit in the business. Here was his need. It called obviously for the formation of a private limited company, and he was accordingly advised that these wishes could be given effect to by a conversion, and that everything would be settled with a minimum of dislocation and expense at a time of his own choice, instead of compulsorily after his decease, when it might be inconvenient, troublesome and costly.

This action was agreed upon, and a valuation of the business was put in hand. A competent valuer was called in to value the land, buildings, plant, machinery, tools, equipment, furniture, fixtures, &c., for the purpose. The auditors examined the books, and certified as to the amount of cash and bank balances, debtors, &c. In due course the valuer's report was received, and it was found that the value was in excess of the book values, largely due to the operation of depreciation over a long period. The book values of the assets were adjusted to conform to the new valuation and the increment credited to the proprietor's capital account. Scrutiny of past accounts had indicated that a certain level of income could be expected. Even on the new value of the assets, the earnings would be sufficient to bear the increased cost of depreciation (a point that must not be overlooked), certain salaries for the proprietor and his sons, and still leave a sufficient margin for the payment of dividends. The scheme that had been prepared was put into action. As this was a case where no new capital was being sought and the interest was a purely family one, no prospectus was required. The business was therefore transferred to the company for an agreed figure representing the net value of the property passing to the company. This value was based, as I have already said, upon a valuation of the assets and upon the book figures, and no amount was included for goodwill. The proprietor, who thus became the vendor, received this sum entirely in shares of the company. In cases like this it is not essential that everything belonging to the business or used in connection with it should be handed over to the company, and in practice it is the case occasionally that certain assets are retained by the vendor. For example, book debts may not be transferred, but merely collected by the company on his behalf. The vendor may transfer the business and plant, and yet remain owner of the premises granting a lease to the company. The agreement for sale of the business is prepared by the solicitor, who, in collaboration with the accountant, will also have drafted the Memorandum and Articles. In the cases of small companies, it is much the cheaper method to utilise Table "A," and make the necessary adjustments or alterations to fit the circumstances than for a complete and original draft of the Memorandum and Articles to be prepared. In the example that I have been referring to, the nominal capital was fixed at £10,000, divided into 4,000 preference shares and 6,000 ordinary. The agreement for sale fixed a price of £9,300 as the purchase price, and this value in shares was allotted to the vendor or his nominees as he might direct. The manner in which the vendor's requirements as regards his wishes were met was as follows:—1,500 preference shares were allotted to each of his two daughters, and 300 preference shares to each of his three sons. In addition, the latter had 800 ordinary shares allotted to each, making a total of 3,900 preference and 2,400 ordinary. The vendor took the balance of the purchase price as 3,000 ordinary shares. By the Articles of Association the vendor was appointed governing director during his lifetime, and as he was still in control by virtue of his governing directorship and his majority of ordinary shares, the salaries of his sons and the management of the business generally was determined exactly as they had been previously.

It can be assumed, as it was the case, that his income from the business previously had been in excess of his requirements. Upon giving his daughters an income directly from the business by their holding of preference shares, he reduced or eliminated the former allowance he had been in the habit of making, so that though he had distributed to his children a large proportion of his capital, the reduction in his actual income was not more than he could quite comfortably manage.

I ought to tell you that in conjunction with this scheme he drew up a new will, whereby he left a life interest in the whole of his then estate to his widow, and thereafter equally between his children, so that subsequently each

received (on their mother's death) 600 ordinary shares, plus one-fifth of his other estate. At his death the value of the ordinary shares, except for purposes of estate duty, did not affect the interest of his children. Their portions being all pre-determined, the death of the governing director did not cause immediate confusion. There was no inconvenience owing to closed bank accounts until probate was obtained, and there was no necessity to call in a valuer at what is always an inconvenient time, and all possibility of argument amongst the members of the family as to who was to take over the business and at what price was entirely eliminated. As the governing director at his death held only ordinary shares, the registration of the necessary transfer to his executors was all that was needed. The remaining directors continued to carry on the business. The subsequent realisation by any beneficiary under the will of his or her shares is, of course, one entirely of agreement between a buyer and seller of a price per share. In any such similar case as I have just outlined, I would always urge the conversion of a business into a limited company. The advantages appear to me to be too great to be ignored.

SECOND EXAMPLE.

I come now to my second example, where the considerations were rather different. Two men, one married and one single, had commenced a business. They had pooled their available capital, but commenced business in the main upon borrowed money. I may say that their united capital, including borrowings, which were the major portion, came to £500. They rented premises, and for a period of three years worked together harmoniously. As demonstrating what ability, knowledge of their work, and courage can do, by the end of that time they had worked up a good business, had removed within the last twelve months to freehold premises, they had lived quite comfortably, I believe, upon their drawings, they had repaid the whole of their original borrowings, and their joint capital in the concern stood at a total of £1,500.

Then came a split. The younger single man desired to dissolve partnership and go to another town. As the result of arbitration, the price of his share was fixed at £1,200. This figure was beyond the capacity of the remaining partner to provide—and as a solution of his difficulty the idea was broached and accepted of the formation of a private limited company in order to provide the means of financing the payment off of the younger partner. The preparation of the scheme was put in the hands of the firm's accountants. The scheme did not provide, in this instance, for any valuation by a valuer, as, owing to the so recent acquisition of the freehold premises, it was considered that the then book value of the property was sufficiently correct. Stocks were carefully taken, and a valuation made of the goodwill. A prospectus (for issue only to friends and customers) was very carefully drawn up, giving all the necessary details—history of the firm, proposed directors, auditors, solicitors, management, past results, reason for formation, future prospects, &c., and sent to selected customers and friends with a view to ascertaining what support could be obtained as regards capital if the company were formed. Advantage was taken of the opportunity to seek additional capital in order to provide funds for building a new showroom, offices and other accommodation, and providing more working capital. The nominal capital was fixed at £5,000, divided into 3,000 preference shares and 2,000 ordinary. The response was very satisfactory, and practically the whole of the preference shares were subscribed for. The vendor, *i.e.*, the remaining partner, took the whole of his interest in ordinary shares. The company was duly formed, the existing business was thereby converted, and it has operated successfully and profitably since. In this case, therefore, the following requirements were met:—capital was obtained to pay off a retiring partner, additional capital was found for extension, the remaining partner's income was increased, and he still retained complete control of his business.

THIRD EXAMPLE.

Now my third example is more general in character, and I hope to indicate the points which need special attention rather than give you a lot of detail about the purely formal side of a conversion. I will now assume that we have under consideration the question of the conversion of a business into a public company. Herein, of course, the factors that are to be considered are considerably more numerous and individually of greater importance. The reasons for conversion I have already outlined. Whatever these reasons may be, they must of necessity be fully determined before any scheme can be prepared. You may perhaps think that I am attaching a great deal of importance to this matter of reasons. Well, I think they are important, because though the actual process of conversion is much the same in all cases, the final product of the conversion must be in such form as will facilitate the carrying out of, or give effect to, the real reasons for which the company is brought into existence.

When the business to be converted is not in need of financial assistance, then the business will simply be transferred to the company for an agreed sum representing the value of the property passing to the company. This value will be determined in the usual way by the valuation of the different assets according to their nature. Land and buildings, plant, machinery and the like should all be valued by a competent firm of valuers. Stocks will be valued either by valuers or by the management, and the valuations examined and checked by the firm's accountants. Bank balance will be certified by the bankers and confirmed by the firm's auditors from the books of the company, and the latter will likewise verify and certify as to the other balances shown by the books, cash, debtors, unexpired amounts, and so on. Goodwill should also be valued by the accountants. Investments quoted on the Stock Exchange should be valued by a stockbroker, and unquoted investments upon information received as to their value from other sources. Investments in subsidiary firms or companies will be valued by the firm's accountants, basing their valuation on information and examination of the subsidiaries' books, supported in turn by valuations of assets in similar manner to the parent firm.

The Memorandum and Articles of Association must be very carefully drawn up, and it is advisable that such matters should be entrusted to a firm of solicitors who are specialised in company work. The Memorandum and Articles constitute the charter of existence of the company, and it is essential that they should contain all the necessary powers that may be required in order to give full effect to the reasons for which the company is called into being. Although the actual preparation of the Memorandum and Articles should be done by the solicitors, they should observe the closest collaboration with the accountants, especially as regards powers and regulations which concern the financial or accountancy side of the business.

The solicitors must also prepare the necessary agreements for sale or transfer of the assets, service agreements with managers, &c., where desirable. If the objects of conversion also include the seeking of fresh capital by public subscription, then further agreements will probably be required according to the nature of the scheme—

agreements regarding the placing and issue of a prospectus, payment of preliminary expenses, promotion costs, &c.

Some of you will perhaps remember that in my previous lecture on "Amalgamation of Companies" I suggested that there should be a sort of "O.C. of Amalgamation Matters," upon whom would devolve the actual carrying through of the amalgamation. In the case of the conversion of a business into a limited company, I would similarly urge the necessity or advisability of having a similar person in charge of all conversion matters. Perhaps to a very large extent the individual who is already termed a "promoter" acts in the capacity I suggest, but not necessarily—the promoters of a limited company may quite possibly be the present proprietors of a business; in other words, the partners may be the promoters, but they would quite probably not be the best people to handle a conversion scheme themselves. A conversion is out of their ordinary occupations, and it involves a considerable knowledge of finance, accountancy, law, and the methods by which the public's interest can be directed to the proposed formation, which they probably do not possess. The ideal plan, I submit, is for them to appoint someone outside their own business to handle the scheme for them—and to see it through in all details. In my opinion, this is work for which a qualified and experienced accountant is eminently suitable. I might perhaps add that the remuneration for such services should be on a liberal basis in view of the special nature of the work to be performed. This expense will be well worth incurring, and will prove to be really only a small portion of the total cost of the conversion.

If the conversion scheme is to include the seeking of new capital from the public, then it becomes necessary to do a number of things which do not necessarily occur otherwise. Let us assume for a moment that the scheme has been formulated and approved by the heads of the present business. For one thing, some outside directors may be required. This necessitates innumerable interviews with people whom it is desired to interest in the scheme, either for their financial support, or their technical skill, or their knowledge and experience, or for their influence. Every such potential director will require to be told, informed and primed with details of the scheme, past results, prospects, &c., until the promoter succeeds in his task or gives it up as hopeless. There is also the question of dealing with the issue of new capital. For this it is almost a necessity to approach what is known as an "issuing house," in order to get the matter handled. The best method of approach is probably through some stockbroker, who can recommend either one of the merchant brokers who handle these propositions, or one of the many excellent trusts which also transact this type of business. They are in touch with the latest financial conditions, and are well able to judge the pulse of the financial world. It is to such that one would look for guidance as to the best terms on which to offer the new capital for subscription, and they would also advise as to the most suitable date on which to issue the prospectus. Such people will also require convincing of the merits of the business to be converted, and they may also stipulate for certain alterations to be made in the scheme in order to ensure a successful flotation. Underwriting arrangements, when required, are usually left in their hands. The bankers of the business will require to be interviewed and consulted, as their co-operation is necessary in handling a flotation—the same applies to stockbrokers (if any are officially appointed)—and full and proper arrangements may require to be made with transfer registration agents. The actual procedure of conversion consists chiefly in the formation of the limited company. This is effected by the filing of various documents consisting of printed copies of the Memorandum and Articles of Association, statement of the nominal capital, notice of situation of the registered office, particulars of directors, and a prospectus; also the payment of various filing fees and the *ad valorem* stamp duty on the nominal amount of the capital, &c. The Memorandum and Articles must, of course, be signed by seven persons, seeing that the company is to be a public one—the other forms must be signed by the directors. Upon the documents being lodged at the Companies' Registry, they are examined by the Registrar, and if no question arises they are provisionally accepted on payment of the duty and fees. A few days later they are again subjected to a second scrutiny, and if they are then passed, the Registrar issues his Certificate of Incorporation bearing the date of the day of payment and the amount of the duty and fees. The 1929 Act, sect. 94, restricts a company having a share capital which issues a prospectus inviting the public to subscribe for its shares, from commencing business or exercising its borrowing powers until the obligations set out in the section have been complied with. There is under the section no restriction as heretofore on the commencement of business or necessity for a trading certificate by a company which has not a share capital. Until this section has been complied with, the conversion cannot be said to have been completed.

I have endeavoured in this lecture to deal with the subject of conversion more from the aspects requiring consideration, thought and skill, rather than from a, shall I say, purely academic and technical point of view—not so much, in fact, from the actual handling of the conversion, as to the points to which attention and care have to be given. I hope that I have succeeded in some way in conveying my ideas to you.

Incorporated Accountants' Students' Society of London.

Syllabus of Lectures—Autumn Session, 1932.

Oct. 5th. Lecture, "Recent Developments in Mercantile Law," by Mr. Maurice Share, B.A., Barrister-at-Law. *Chairman:* Sir Stephen Killik, J.P., President of the Society.

Oct. 11th. Lecture, "Some Monetary Problems," by Mr. H. E. Davis, Incorporated Accountant. *Chairman:* Mr. W. H. Coates, Ph.D., LL.B.

Oct. 18th. Lecture, "The Accounts of Holding Companies," by Mr. A. E. Langton. *Chairman:* Mr. Richard A. Witty, F.S.A.A.

Nov. 8th. Lecture, "The Economic War," by Mr. S. W. Alexander, City Editor, *Daily Express*. *Chairman:* Mr. E. Cassleton Elliott (President, Society of Incorporated Accountants and Auditors).

Nov. 15th. Lecture, "Railway Accounts," by Mr. R. G. Davidson, Incorporated Accountant (Joint Accountant, Southern Railway Company). *Chairman:* Mr. Wm. Strachan, F.S.A.A.

Dec. 6th. Professor Gregory will give a Lecture to the Incorporated Accountants' London and District Society, the subject of which will be announced later. Members of the London Students' Society are cordially invited to attend.

Scottish Notes.

(FROM OUR CORRESPONDENT.)

Scottish Committee on Local Expenditure.

The Scottish Committee on Local Expenditure appointed by the Government is a very representative one. The following are the members: Lord Lovat, K.T.; Sir Henry Keith, LL.D.; Mr. J. M. Hodge; Mr. L. S. Gumley; Mr. George D. Morton; Provost Henry Smith, C.A.; Provost J. R. Rutherford, J.P., F.C.I.S.; Mr. Ian Carmichael. A preliminary meeting was held last month in Edinburgh.

Sir John Lamb, K.C.B., Under-Secretary of State for Scotland, presided at the commencement of the meeting, and apologised for the unavoidable absence of Sir Archibald Sinclair, Secretary of State for Scotland. Sir John explained the purposes of the Government in setting up the Committee.

The meeting appointed Lord Lovat to be Chairman and Sir Henry Keith Vice-Chairman. The Chief Accountant of the Department of Health for Scotland and President of the Scottish Branch, Mr. J. Stewart Seggie, F.S.A.A., C.A., was appointed Secretary to the Committee.

Important Rent Decision.

A point of considerable importance regarding the issue of a certificate of disrepair in respect of a dwelling-house in Glasgow has been decided by Sheriff Bartholomew. The factors for a body of trustees raised an action against a tenant for arrears of rent. It was admitted that the rent was due, but the tenant pleaded that, under sect. 5 (1) of the Rent and Mortgage Interest (Restriction) Act of 1923, he was entitled to withhold the rent on account of the disrepair of the house.

This section provides that, if the tenant had obtained from the sanitary authorities a certificate that the house was not in a reasonable state of repair and had served a copy of such certificate on the landlord, it should be a good defence to any claim against the tenant for payment of any increase of rent.

The tenant also served on the landlord a certificate by the Medical Officer of Health for Glasgow that the house was not in all respects reasonably fit for human habitation, and was not capable at a reasonable expense of being rendered so fit.

The Sheriff held that this was not a valid certificate, as sect. 18 (1) of the 1923 Act provided that the certificate should specify what work, if any, required to be executed in order to put the house into a reasonable state of repair. It was not for the local authority to say that the repairs could not be done at a reasonable expense. The certificate not being in the form prescribed by the Act, the Sheriff held that a defence could not be founded on it, and that the pursuers were entitled to decree.

Local Economy.

At the summer school for Scottish Local Government Officers, held at St. Andrews at the end of July, Mr. J. D. Imrie, F.S.A.A., City Chamberlain of Edinburgh, in closing the session, discussed the problem of the attainment of a reasonable figure of economy in local administration. He said that this could only be secured if there was within the local government machine an organisation charged with the duty of making economy one of its principal objectives. The legislature had provided for an annual audit of accounts being prepared, published and made available for inspection by ratepayers. These accounts were prepared in a standard form, an attribute of Scottish local government not found in English practice.

It would be a great advantage, continued Mr. Imrie, to have a common financial code for all local authorities, which would, *inter alia*, make provision for a properly functioning finance committee to correlate the financial activities of each local authority. The finance committee could direct the attention of its authority to innovations in expenditure and to the scale of activities of departments. The committee would correlate the budget both for capital and for ordinary expenditure, and would present estimates to the local authority in a form in which they could be easily grasped. All structures of Government were stronger if there was in existence a check against hasty and extravagant action.

In order that proper correlation of the financial activities of the several departments should be reached, it was suggested that there should be a treasurer or some person occupying the position of chief financial officer, properly equipped for the duties which were allocated to him, and recognised as holding the position of the chief financial officer, directly responsible to the Council.

Until that stage was reached, and it had not been reached in many of the authorities to-day, it was difficult to see how the machine of local government could continuously and effectively function in the direction of economy.

Interesting Succession Case.

The Second Division of the Court of Session recently advised a reclaiming note in an action of multiple poinding in which the question was whether or not the universal testamentary disposition, dated February 15th, 1928, and executed by William Stevenson, sometime of Kingarth, Hamilton, and thereafter of Prestwick, was his effective testament and disposition of heritage. Mr. Stevenson was married three times. He died on August 12th, 1930. A son was born on November 14th, 1928. The trustees in this action sought to obtain judicial determination of the question whether William Stevenson's settlement was revoked by the birth of a child of his marriage after the date of the deed. The child, on whose birth subsequent to the date of the settlement the question depended, was not a party to, nor represented in, the action.

In the Outer House Lord Mackay held that, as the testator did not make a new will after the birth of the child in question, he had left himself intestate. This seemed rather a peculiar view.

The Division unanimously sustained the appeal, recalled the judgment of the Lord Ordinary, and sustained the claims of those who maintained the settlement in dispute.

The Lord Justice-Clerk, in the course of his opinion, asked the preliminary question—Could a stranger challenge the validity of a will, basing his challenge on the doctrine of the *conditio si testator sine liberis decesserit?* That was what the heirs-at-law sought to do in this case. His Lordship had always understood that the doctrine of the *conditio* was founded on equity, and that it operated for the amelioration of the hardship created to a subsequently-born child by reason of the provisions of a settlement which was executed before his birth, and which did not contemplate his existence. The underlying doctrine, he apprehended, was that the testator would not have made the will which he did had he contemplated the subsequent birth of issue. *Prima facie*, then, the right of challenge would seem to reside in the person for whose benefit the doctrine was introduced, namely, the after-born. That view would seem to be strengthened by the fact that, in the long history of Scots law, no case was recorded in which a stranger to a settlement had been allowed to plead the *conditio*. Indeed, there was, so far as his Lordship knew, no record of such an attempt having been made. In every case where a decision relating to the *conditio* was given the child was a party to the process as a claimant. After examining the authorities, his Lordship said the cumulative force of those views was so compelling as to leave no doubt in his mind that a challenge of a will on the ground of

the *conditio* was open only to the disinherited child, and that it was not open to a stranger.

Incorporated Accountants' Golf Club.

The next competition for the Dunlop Cup will take place on September 3rd at Lochgreen, Troon, course.

Notes on Legal Cases.

[The abbreviations at the end of each of the cases refer to the following law reports, where full reports of the case may be found. The Law Reports and other reports are cited with the year and the Division, *e.g.* (1925) 2 K.B. :—

T.L.R., *Times Law Reports*; *The Times*, *The Times* Newspaper; L.J., *Law Journal*; L.J.N., *Law Journal* Newspaper; L.T., *Law Times*; L.T.N., *Law Times* Newspaper; S.J., *Solicitors' Journal*; W.N., *Weekly Notes*; S.C., *Session Cases* (*Scotland*); S.L.T., *Scots Law Times*; I.L.T., *Irish Law Times*; J.P., *Justice of the Peace* (*England*); L.G.R., *Knight's Local Government Reports*; B.&C.R., *Bankruptcy and Company Cases*.

The other abbreviations used in modern reports are H.L., House of Lords; A.C., Appeal Court (House of Lords and Privy Council); C.A., Court of Appeal; Ch., Chancery Division; K.B., King's Bench Division; P., Probate, Divorce and Admiralty Division; C.S., Court of Session (Scotland); J., Mr. Justice (King's Bench or Chancery); L.J., Lord Justice; L.C., Lord Chancellor; M.R., Master of the Rolls; N.I., Northern Ireland; P., President of Probate, Divorce and Admiralty.]

COMPANY LAW.

In re Airedale Garage Company, Limited.

Preferential Debts.

The Court of Appeal reversed the decision of Eve (J.) (see *Incorporated Accountants' Journal*, July, p. 404), and held that if premises of a company have been derated as being an industrial hereditament under the Local Government Act, 1929, and the derating has been cancelled after the company owning the premises has gone into liquidation or a receiver has been appointed, the extra rates imposed rank as a preferential debt within sect. 264 of the Companies Act, 1929, if the original rate was duly made and published within twelve months before the commencement of the winding up or the appointment of the receiver, as the case may be.

(C.A.; (1932) 48 T.L.R., 477.)

British Thomson-Houston Company, Limited, v. Federated European Bank, Limited.

Delegation of Powers to Director.

By the Articles of Association of a company the directors had power to delegate to one or more of their own body such of the powers conferred on the directors as they might consider requisite for carrying on the business of the company, and to determine who should be entitled to sign contracts and documents on the company's behalf. A document purporting to be a guarantee was given to the plaintiffs executed by the company in this form: "The F.E.B., Ld, signed N.P." N.P. was a director of the company. During the negotiations for the giving of the guarantee he had written to the plaintiffs, signing the letter "for and on behalf of" the company, "N.P., Chairman."

It was held that the plaintiffs were entitled to presume that the directors had authorised N.P. to sign contracts on behalf of the company, and that the company was liable on the guarantee.

(K.B.; (1932) 2 K.B., 176.)

INSOLVENCY.

Rex v. Zeitlin.

Undischarged Bankrupt Obtaining Credit.

By sect. 155 of the Bankruptcy Act, 1914, where an undischarged bankrupt obtains credit to the extent of £10 or upwards from any person without informing that person that he is an undischarged bankrupt, he is guilty of a misdemeanour.

If he gives information to a creditor a reasonable time before he obtains the credit, he is not within sect. 155. The information need not necessarily be given at the moment of obtaining the credit.

(C.C.A.; (1932) 23 Cr. App., 163.)

MISCELLANEOUS.

Rekstin v. Komseverputj Bureau and Bank for Russian Trade Limited.

Service of Garnishee Order on Bank.

Judgment debtors instructed their bank to transfer their current account balance to the Russian Trade Delegation and to close the account. At 3 p.m. the bank had made out the slip carrying out the transaction and had made the book entries, but shortly afterwards the judgment creditor served the bank with a garnishee order *nisi*, attaching the account.

It was held by the Court of Appeal, affirming the decision of the Divisional Court (see *Incorporated Accountants' Journal*, July, 1932, p. 404), that as the evidence showed that the proposed transferees had no knowledge of the transaction and therefore could not have assented to it, the mere entries in the bank's books did not complete the transfer, and the bank, therefore, still owed the judgment debtors and the garnishee order operated as a mandate to attach the account.

(C.A.; (1932) 48 T.L.R., 578.)

Greenwood v. Martin's Bank.

Signature on Cheques Forged by Customer's Wife.

The House of Lords affirmed the decision of the Court of Appeal (see *Incorporated Accountants' Journal*, December, 1931, p. 108), and held that where a bank had honoured cheques which were forged by the customer's wife, and the customer with knowledge of the forgery took no action until after his wife's death, that ratification had no application to the case, but that the plaintiff was estopped from alleging the forgeries because his silence until after his wife's death had caused the bank to lose their right of action against the wife and against the plaintiff as her husband.

(H.L.; (1932) 48 T.L.R., 601.)

REVENUE.

Watson's Trustees v. Wiggins.

Income Tax on Settled Fund.

The Court of Appeal dismissed an appeal from a decision of Rowlatt (J.) (see *Incorporated Accountants' Journal*, July, p. 404), and held that as there had been no revocation the annuity was income of the son for purposes of relief from tax, and that the power of revocation did not make it payable for some period less than the life of the child within the meaning of the Finance Act, 1922, sect. 20 (1).

(C.A.; (1932) 2 T.L.R., 654.)

Attorney-General v. Arts Theatre of London Limited.

Entertainments Duty.

The defendants were the proprietors of a club, providing the usual amenities of a social club, and having on the premises a theatre to which members and associate members and their guests, but no others, were admitted

for payment, this payment being in addition to the subscriptions.

It was held that an apportioned part of the subscriptions was chargeable with entertainments duty ,as the payment of the subscriptions was to be attributed in part to the purchase of a right to purchase tickets for the entertainments in the theatre.

(K.B. ; (1932) 48 T.L.R., 545.)

Oswald Tillotson, Limited, v. Inland Revenue Commissioners.

Stamp Duty on Reconstruction of Company.

In connection with a scheme for the reconstruction of a company a new company was formed to enter into a sale agreement to acquire the undertaking of the existing company. The consideration for the agreement was to consist (in addition to the discharge by the new company of certain liabilities of the old company) of the allotment of shares in the new company to the shareholders in the old company. Letters of allotment were sent to these shareholders, accompanied by a form of renunciation. Before the original allottees were registered some of them renounced in favour of other persons, with the result that of the first registered shareholders in the new company those who had been shareholders in the old company held less than 90 per cent. of the shares in the new company. The question of the stamp duty payable on the sale agreement and other documents was submitted for adjudication, the company contending that the sending of the letters of allotment constituted an "issue" of shares to the original allottees, and that the conditions of exemption from *ad valorem* duty laid down in sect. 55 of the Finance Act, 1927, were complied with. The Commissioners of Inland Revenue decided that *ad valorem* duty was payable.

It was held that the allotment letter accompanied by the form of renunciation was not an issue of shares, but only notice that the allottee was entitled to demand that shares should be issued either to himself, or, if he preferred it, to his nominee to be named in the form of renunciation. Therefore, though the individual case might be one of hardship, the Commissioners were right in claiming *ad valorem* duty. In other words, to constitute an "issue" of shares the legal and not merely the equitable title must pass.

(K.B. ; (1932) 48 T.L.R., 582.)

Thomas Merthyr Colliery Company, Limited, v. Davis.

Allowable Deductions.

The appellants, a colliery company, were subscribing members of a coalowners' association, which had been formed *inter alia* to indemnify its members against deficiency and stoppage of output by reason of strikes. Part of these contributions was applied by the association as a contribution to the Conciliation Board, and part was contributed to the funds of the Mining Association of Great Britain, which in some matters looked after the interests of coalowners. The appellants claimed that their subscriptions to the association were proper deductions in arriving at their profits.

It was held that the appellants were not entitled to deduct that part of their subscriptions which was applied towards an indemnity against loss of output by reason of strikes and to the funds of the Mining Association, but that they were entitled to deduct the part which was applied as a contribution to the Conciliation Board.

(K.B. ; (1932) 48 T.L.R., 476.)

Attorney-General v. Adamson.

Property Passing on Death.

By a settlement, the settlor directed the trustee to hold the capital of the trust funds upon trust for all or such of his children then living or thereafter to be born as he should appoint, and during his life the income pending any such appointments should be accumulated and added to the capital. On his death the capital went as to two-fifths to his son and as to three-fifths equally between his three daughters if they survived him. The trust on the settlor's death in favour of the son was not expressed to be contingent, but there was a proviso that if the son died before the settlor his two-fifths should go over to the daughters, again only in the event of their surviving the settlor. The son and daughters survived the settlor, who had no more children. The question was raised whether on the death of the settlor on March 11th, 1928, without having exercised the power of appointment, the trust property passed on his death to the four children within the meaning of sect. 1 of the Finance Act, 1894, and thus became liable to estate duty, and also devolved on the death so as to create a succession under sect. 2 of the Succession Duty Act, 1853, and was liable to succession duty.

It was held (1) that before the death of the settlor the beneficial interest of the children in the trust property was indefinable, since in certain events they might never have become entitled, and the settlor had reserved full control both of capital and income until his death ; but, on his death, the son became indefeasibly entitled to two-fifths and each of the three daughters became beneficially and indefeasibly entitled to one-fifth, and accordingly the capital of the trust funds passed on the death as also the accumulations of income.

(2) That the capital of the trust funds was also liable to succession duty on the death of the settlor, and that no distinction could be made between capital and accumulations of income which were the fruit borne by the corpus of the settled funds.

(C.A. ; (1932) 2 K.B., 159.)

Morgan Crucible Company, Limited, v. Inland Revenue Commissioners.

Pensions to Retiring Employees.

A company had a scheme under which pensions were paid to its employees who had retired, but reserving an uncontrolled discretion to vary or cease payment of such pensions. The payment of such pensions had ever since been a recurring business expense, and the pensions paid had been debited to the profit and loss accounts under the heading of wages, and were admitted to have been proper deductions in computing the profits of the company for income tax purposes. In 1918 the company entered into an arrangement with an insurance company whereby the latter undertook, in consideration of the sum of £23,100 paid to it by the company, to pay to the company during the remainder of the lives of the persons who were receiving pensions, and who were named in the schedule to the policy, annuities which were equal in amount to the pensions which were being paid by the company in pursuance of its pension scheme. The amounts received from the insurance company under the policy were paid direct to the company, and payments equivalent to the annuities received from the insurance company were made by the company to the pensioners. The company claimed that the sum of £23,100 should be allowed as a deduction in computing the amount of its deficiency for the purposes of excess profits duty for the accounting period ending in 1919.

It was held that the company had not by the payment of £23,100 got rid of their liability to pay the pensions, but had thereby acquired an asset, and that therefore the £23,100 constituted a capital expenditure and could not be allowed as a deduction by reason of rule 3 (*f*) of the Rules applicable to Cases I and II of Schedule D to the Income Tax Act, 1918.

(K.B. ; (1932) 2 K.B., 185.)

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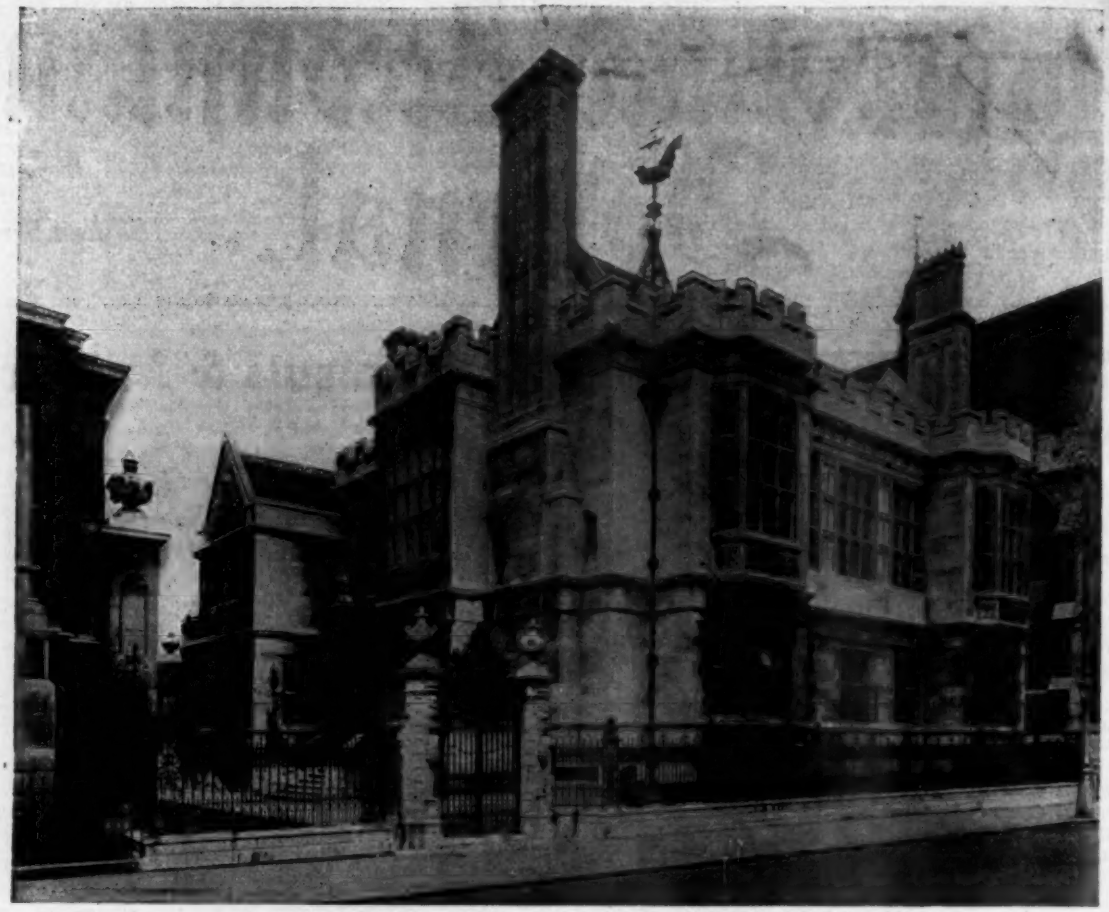

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Again thanking you,
I am, Yours faithfully,
Reference No. C.

Dear Mr. Ludford, *June 28th, 1932.*

I am delighted to be able to inform you that I was successful at the Intermediate Examination of the Society of Incorporated Accountants and Auditors held in May last.

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After my Summer leave (in August) I intend studying for the Final S.A.A. in April next, and in the meantime I would be obliged if you would let me have the prospectus and particulars for this Course.

Yours faithfully,
Reference No. X.

Dear Sir, *June 29th, 1932.*

No doubt you have seen that my son passed the Intermediate Examination of the Society of Incorporated Accountants and Auditors.

I take this opportunity of thanking you and the Staff of the College for their interest during his Course. I think it is a good result to get through at his first attempt and only just 19.

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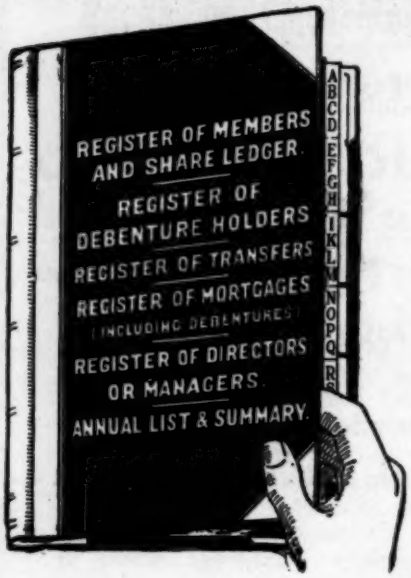

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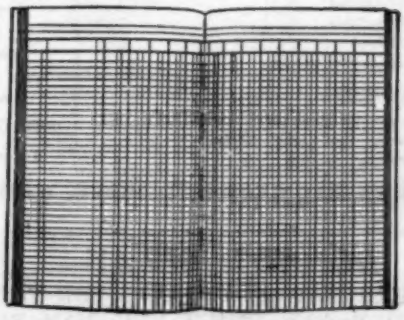

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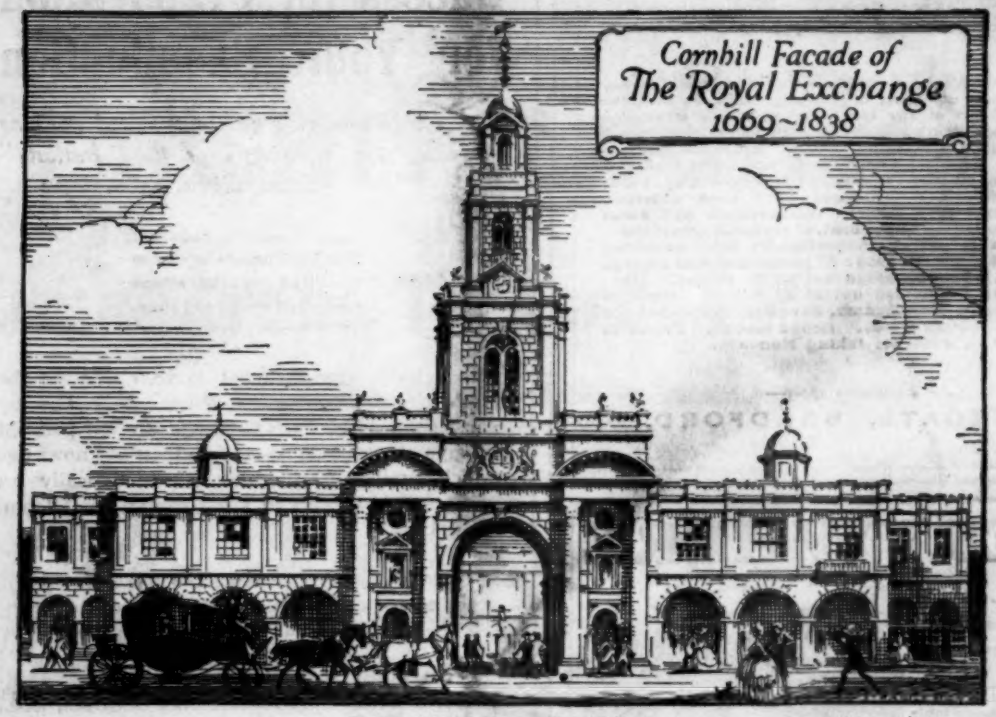

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